OFFICE OF THE CITY AUDITOR

COLORADO SPRINGS, COLORADO

14-26 Answers Concerning City Pensions

October 2014

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Purpose

This report provides informative and comparative data on the pension plans in which the City of Colorado Springs (City) participate. The City of Colorado Springs 2013 Executive Branch Breakthrough Strategies included pension reform as a goal for sustainability and reduced City pension costs. This report is intended to provide City leaders, employees and citizens of Colorado Springs with independent information on the current state, constraints, and health of the City's pension plans.

Key Questions

1. What pension plans are used by the City and does the City control benefits and costs?
Answer: The City uses four different plans to provide pension benefits to employees based on their classification as sworn (fire and police) or civilian, and date of hire. Only the Colorado Springs Old Hire (CSOH) pension plan for sworn employees, which was closed in 1978, is controlled by the City. Benefits for the civilian plan are set by the legislature and overseen by a board. The civilian plan is administered by the Public Employee Retirement Association (PERA). Other sworn plans are administered by the Fire and Police Pension Association (FPPA). The FPPA board includes representation from Colorado employers. The PERA board is composed of elected plan members and three appointees of the governor.

Plan	Active employees on 12/31/13	Employee type	Plan open to new employees?	Does City set plan rules?	2013 contribution rates for employee	2013 contribution rates for employer
PERA	1,325	Civilian	Yes	No	8%	13.7%
Statewide Defined Benefit (SWDB)	476	Sworn	Yes	No	8 or 9.3%[1]	8 or 9.3% [1]
Colorado Springs New Hire (CSNH) Police	446	Sworn	No	No	8 or 9.3%[1]	21.02 or 22.32% [1,2]
Colorado Springs New Hire (CSNH) Fire	184	Sworn	No	No	10 or 11.3%[1]	18.31 or 19.61% [1,2]
Colorado Springs Old Hire (CSOH)	1	Sworn	No	Yes	10%	10% [2]

[1] Lower rates apply to those hired before 1-1-1997 because the State funds the death and disability benefits for those employees.
[2] Additional lump sum payments were made to these plans in recent years which are not included here; see detailed information at report page 5.

2. Are the City pension plans currently financially healthy?
Answer: Overall, we noted plans were healthy or improving in financial health. Currently, the funded ratio for sworn plans exceeds the 80% funded ratio considered by actuaries as a key indicator of financial health. The civilian plan (PERA) was funded at 73.1% as of December 31, 2013. Although the City still has exposure to some of the indicators of troubled plans, we noted the exposure was less than the troubled plans mentioned in this report. We also noted that City pension plans were considered healthy (sworn plans) or improving (PERA) when we considered the reforms noted in this report.

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(Highlights continued from prior page)

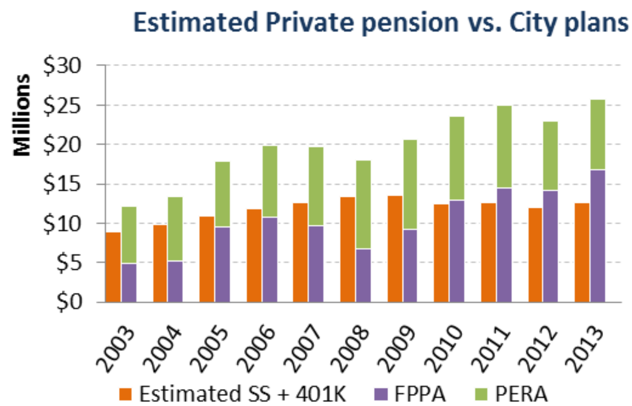
Audit Note: Starting with the 2015 Comprehensive Annual Financial Report (CAFR), new governmental accounting standards will require the City to show any unfunded pension liability on their financial statements.

3. What has been done to improve pension health?

Answer: SWDB plan employee members recently elected to increase their contributions to the plan. Members share of contributions will increase so that member contributions exceed City contributions. City fire and police representatives participated in the task force that recommended additional member contributions. Since 2006, all new sworn employees have been enrolled in the SWDB plan, which has greater plan flexibility, lower contributions and benefits. In 2010, the Colorado Senate introduced reforms to PERA by reducing retiree benefits, which are detailed on page 12. Both PERA and SWDB plans have reduced the impact of cost of living adjustments, made adjustments to ending salary calculations, and increased age or service requirements to receive benefits.

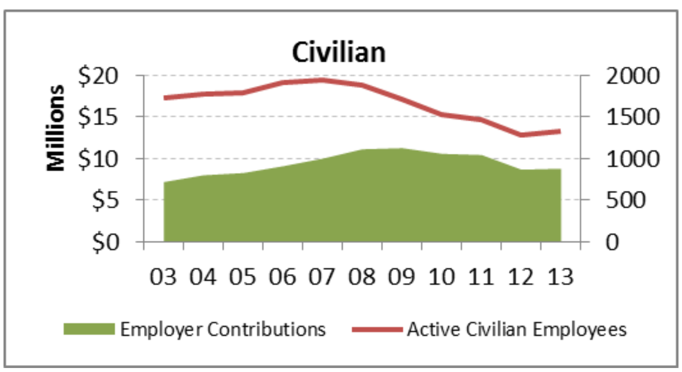
4. How do the City pensions compare to the private sector?

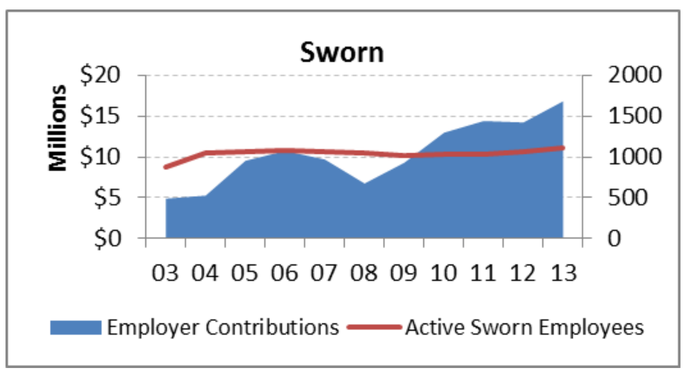
Answer: Employees receive a higher benefit through participation in City pension plans as compared to the private sector. Employees and the City pay more than is required for Social Security. However, depending on the plan provided by a choice employer, the cost to the City for civilian employees may not be significantly higher. See page 13 for more information including assumptions used.



5. What is the total cost of pensions paid by the City?

Answer: Total pension costs paid by the City in 2013 were $25.7 million; $8.9 million for civilian and $16.8 million for sworn. Total employer pension costs have increased 111% since 2003 for all plans combined. Much of the increase was related to CSOH and CSNH pension plans, which were closed .





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Office of the City Auditor
Public Report

Date: October 23, 2014

To: President King, President Pro-Tem Bennett, and Members of City Council

From: Denny L. Nester, City Auditor

Re: 14-26 Answers Concerning City Pensions

This report provides informative and comparative data on the pension plans in which City of Colorado Springs (City) employees participate. The City of Colorado Springs 2013 Executive Branch Breakthrough Strategies included pension reform as a goal for sustainability and reduced City pension costs.

Recognizing national concerns regarding public pension funding, accompanied by the City of Colorado Springs strategic goals for pension reform, this report is intended to provide City leaders, employees, and citizens of Colorado Springs with independent information on the current state, constraints, and health of the City's pension plans. Our report includes actuarial data from plan administrator annual reports, but our review did not include actuarial analysis. The scope of our review included pension contributions, but did not extend to other post-employment benefits such as retiree health care.

The City uses four plans to provide pension benefits to employees based on their classification as sworn (fire and police) or civilian, and date of hire. The City and City employees do not pay into Social Security. The City controls the benefit for the Colorado Springs Old Hire (CSOH) plan. Benefits for the civilian plans are set by the legislature and overseen by a board. The civilian plan is administered by the Public Employee Retirement Association (PERA). Other sworn plans are administered by the Fire and Police Pension Association (FPPA). The FPPA board includes representation from Colorado employers. The PERA board is composed of elected plan members and three appointees of the governor.

Overall, we noted City plans were healthy or improving in financial health. City PERA and Statewide Defined Benefit (SWDB) pension plans have been reformed in recent years to improve pension health. In comparing City employee costs and benefits to the private sector, we found City employees receive a higher retirement benefit as compared to the private sector. We also found City pension plans require employees to contribute more than the private sector. City employees contribute between 8% and 11.3% as compared to 6.2% that private sector employees contribute for social security. Only a few executives or officials, who are not covered by the plans discussed in this report, pay into social security.

The total wages paid to City employees in 2013 was $137.7 million. The total pension costs paid by the City in 2013 were $25.7 million. Total employer pension costs have increased 111% since 2003 for all plans combined. Approximately 88% of the $13.5 million increase in pension costs from 2003 to 2013 was in fire and police plans.

As always, feel free to contact me if you have any questions.

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REPORT DETAILS

PURPOSE AND SCOPE

The purpose of the review was to provide informative and comparative data on the City of Colorado Springs (City) pension plans. The City of Colorado Springs 2013 Executive Branch Breakthrough Strategies included pension reform as a goal for sustainability and reduced City pension costs. Recognizing national concerns regarding public pension funding, accompanied by the City of Colorado Springs strategic goals for pension reform, this report is intended to provide City leaders, employees, and citizens of Colorado Springs with independent information on the current state, constraints, and health of the City's pension plans.

This report does not include analysis of future City pension plans costs or Colorado Springs Utilities pension costs. Our objective and review did not include actuarial valuation of plan funding. Our report includes actuarial data from plan administrator annual reports, but our review did not include further actuarial analysis.

The scope of our review included pension contributions, but did not extend to all post-employment benefits. We included the cost of death and disability benefits for all employees. However, the civilian and sworn plans differ in that the civilian contributions include post-retirement health care. Post-retirement health care benefits for sworn employees are paid and administered directly by the City and the costs of these benefits were not addressed in this report. We compared the costs of the civilian and sworn plans to the private sector using several assumptions.

CONCLUSION

Overall, we noted City plans were healthy or improving in financial health. City PERA and SWDB pension plans have experienced reforms in recent years that have or will improve pension health. In comparing City employer and employee costs and benefits to the private sector, we found City employees receive a higher retirement benefit and make higher required contributions as compared to the private sector. The City and City employees do not contribute to Social Security.

Total pension costs paid by the City in 2013 were $25.7 million. Total City pension costs have increased 111% since 2003. Approximately 88% of the $13.5 million increase in pension costs from 2003 to 2013 was in sworn plans. Much of that increase was related to the CSOH and CSNH pension plans, which are closed and have higher costs for the employer as compared to PERA.

BACKGROUND

The information concerning City pensions in the remainder of this report are organized into five questions. An overview of information presented to answer each question is provided below with the full details in the remainder of this report.

Question 1: What pension plans are used by the City of Colorado Springs and who determines benefits and costs?

- Active number of employees by plan
- Who controls or sets the plan costs and plan benefits
- Historical information on the three sworn pension plans
- Pension term definitions
- Vesting information for each plan
- Employee and employer annual contribution rates

Question 2: Are the City pension plans financially healthy?

- Three key measures of financial health identified(Funding Ratio, Investment Rate of Return and Amortization Period)
- Funding ratio by plan from 2001 to 2013
- Investment rate of return by plan (actual 2003 to 2013 and future assumed rate)
- Amortization period by plan
- Comparison of City pension plans to nationally publicized troubled plans
- New governmental accounting standard related to pension plan liabilities

Question 3: What has been done to improve pension health?

- PERA plan key reforms passed by state legislature
- Reforms to the SWDB plan
- Estimated impact of reforms and plan changes chart

Question 4: How do the City plans compare to the private sector?

- Private sector employer compared to City pension costs with calculation assumptions
- City wage and pension costs
- Average salary and benefit of 2013 retirees

Question 5: What is the total cost of pensions paid by the City?

- Civilian pension costs
- Sworn pension costs
- City budget compared to wage and pension costs
- Employer and employee pension contributions

#1 – What pension plans are used by the City of Colorado Springs and who determines benefits and costs?

- **The City uses four different plans to provide pension benefits to employees based on classification as either sworn (fire or police) or civilian, and date of hire.**
- **Only the CSOH pension plan for sworn employees, which was closed in 1978, is controlled by the City. Benefits for the civilian plans are set by the state legislature and overseen by a board. The civilian plan is administered by PERA. The sworn plans are administered by FPPA.**
- **Although the City does not determine benefits and rules, Colorado employers are included on the FPPA board. Colorado employers are not represented on the PERA Board.**

Plan	Active employees on 12/31/13	Employee type	Plan open to new employees?	Does City set plan rules?	2013 contribution rates for employee	2013 contribution rates for employer
PERA	1,325	Civilian	Yes	No	8%	13.7%
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[1] The lower rate applies to those hired before January 1, 1997. The State funds disability and death benefits for those hired before January 1, 1997.
[2] Additional required lump sum payments were made to these closed plans in 2013. See details of employer contributions on page 5.

Public Employee Retirement Association (PERA)

Who participates: Civilian employees

Who controls: Colorado Legislature and PERA Board

Vesting period: 5 years – see defined terms on right

Active employees: 1,325

Since the City became a member of PERA in 1944, state law requires PERA membership as a condition of employment for civilian municipal employees. Elected officials, and certain executives are exempt from this requirement and may elect to participate in an alternative defined contribution plan.

PERA is a cost sharing, multiple-employer, defined benefit pension plan. For funding purposes, PERA is made up of five divisions: Local Government, State, School, Judicial, and Denver Public Schools. Employees of the City of Colorado Springs are members of the Local Government division of PERA.

Colorado PERA operates by authority of the Colorado General Assembly and is administered under Colorado Revised Statutes. Benefits, contribution rates and some investment parameters are legislated by the Colorado General Assembly.

The PERA board is composed of elected plan members and three appointees of the governor.

Defined Terms –

Pension – a retirement benefit plan offered to employees by an employer. Employees and/or employer make periodic payments toward the investment fund. After retirement, the employee typically receives a monthly payout.

Active employee – an employee currently contributing to the plan. Retirees do not make contributions but receive benefits.

Unfunded liability – The share of all pension benefits earned by current and former employees that cannot be covered by current assets based on a set of assumptions.

PERA – Colorado Public Employee Retirement Association.

FPPA – Fire and Police Pension Association of Colorado.

Funding ratio – A plan's current assets as a percentage of liabilities based on a set of assumptions.

Vesting – The process by which an employee becomes entitled to the contributions the employer has made to the plan.

Defined benefit plan – A type of retirement plan that invests employer and/or employee contributions and provides a regular post-retirement payment for life, typically based on a formula calculated using years of service, salary, and a multiplier.

Fire and Police Pension Association of Colorado (FPPA) - Statewide Defined Benefit (SWDB) Plan

Who participates: Sworn employees hired on or after October 1, 2006

Who controls: FPPA Board

Vesting period: 5 years

Active employees: 476

Police and fire personnel hired on or after October 1, 2006, are covered under the SWDB Plan. The City provided two windows of opportunity for members of older plans to voluntarily transfer to the SWDB Plan.

FPPA is governed by a nine member board of directors who are appointed by the governor and confirmed by the state senate. Board composition includes both employee and employer representatives from municipal districts across the state. The board of directors is responsible for investing and managing the benefit fund and setting required contribution levels for retirement benefits.

Colorado Springs New Hire (CSNH) Plan

Who participates: Sworn employees hired after 1978 but before October 1, 2006

Who controls: FPPA Board

Vesting period: 10 years

Active employees: 630

In 1978, the City established the CSNH plans (one police, one fire) as a replacement for the older sworn plans. The two CSNH plans have different requirements for retirement and associated benefits. Initially, the city chose to establish and maintain its own CSNH plans rather than joining the SWDB plan. Effective October 1, 2006, the CSNH Pension Plan became a part of the FPPA, an association organized to administer multiple employer public employee retirement systems for State of Colorado police and fire personnel.

Colorado Springs Old Hire (CSOH) Plan

Who participates: Sworn employees hired before 1978

Who controls: Colorado Springs

Vesting period: 20 years

Active employees: 1

The CSOH plan was established by the City in the early 1900s. By the late 1970s, the plan faced a large unfunded liability and was closed to new members in 1978. From 1978 to 1998, the City and state appropriated millions of dollars as special additional contributions to this plan in order to eliminate the unfunded liabilities. At times, the city contribution for this plan approached 50% of covered salary. Today, the City contributes 10% of an employee's salary and makes lump sum payments to fund the annual required contribution per the biennial actuarial studies. While the City maintains responsibility for the CSOH plan, it is administered jointly by FPPA along with the other sworn plans.

Vesting

Plan	Vesting Period
PERA	5 years
SWDB Plan	5 years
CSNH Plan – Both Fire and Police	10 years
CSOH Plan	20 years

Under PERA, A City employee is eligible to receive a "full" monthly retirement benefit, up to 100% of highest average salary (HAS), if he or she has 40 years of service. Similarly, the SWBD plan compensates at 100% of HAS after 42 years. A "reduced" retirement benefit can be received with fewer service years. The maximum benefits and requirements for retirement vary between plans.

Employees who separated employment prior to retirement

With less than five years of service, PERA and SWDB plan employees can receive a reduced pension benefit based only on the employee's contributions (plus any earnings). Upon leaving employment the employee can also refund or rollover their account (their portion of contributions) while the City's contribution portion will remain with PERA or FPPA.

With five or more years of service but less than full retirement, upon separation the employee may leave the account with PERA or SWDB plans and at a certain age receive a partial monthly benefit calculated on years of service, age and highest average salary. Alternatively, the employee can roll over or refund the account balance comprised of the employee's contributions and 100% of the employer's matching contribution. To receive this benefit in the CSNH plan, the employee must have 10 years of service.

PENSION PLANS - CONTINUED

Pension Plans and Social Security

Typical City employees are not eligible to participate in Social Security. The City does not pay into Social Security except for a few executives and elected official. Only City employees who paid into Social Security while working for other employers may receive social security benefits. If the employee is entitled to benefits from both Social Security and a municipal pension plan, the Social Security benefit may be reduced under the Windfall Elimination Provision (WEP). Social Security benefits will not be reduced if the employee has 30 years of substantial earnings under Social Security.

EMPLOYER CONTRIBUTION RATE

CIVILIAN

Currently, the City contributes a total of 13.7% of civilian payroll to PERA according to state law. This rate includes a 10% base rate and additional contributions of 3.7%. In 2004 and 2006, legislation passed requiring employers to remit additional contributions of 2.2% for Amortization Equalization Disbursement (AED) and 1.5% for Supplemental Amortization Equalization Disbursement (SAED) designed to reduce PERA's unfunded liability and amortization period.

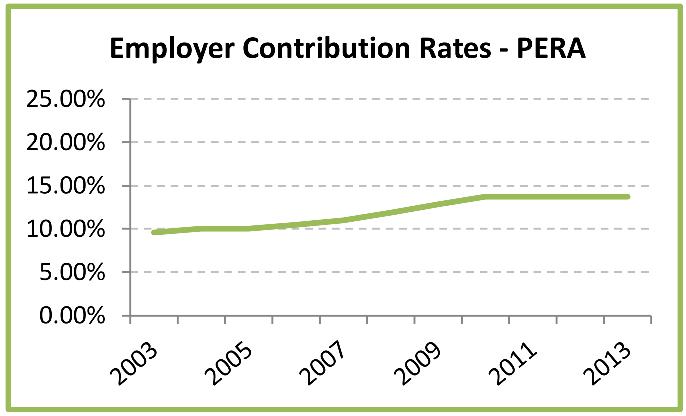
A portion (1.02%) of the employer contribution goes to the Health Care Trust Fund (HCTF) to pay health care premium subsidies for benefit recipients. While PERA provides short-term disability and disability retirement programs for vested employees, no special contribution is required from the employer.

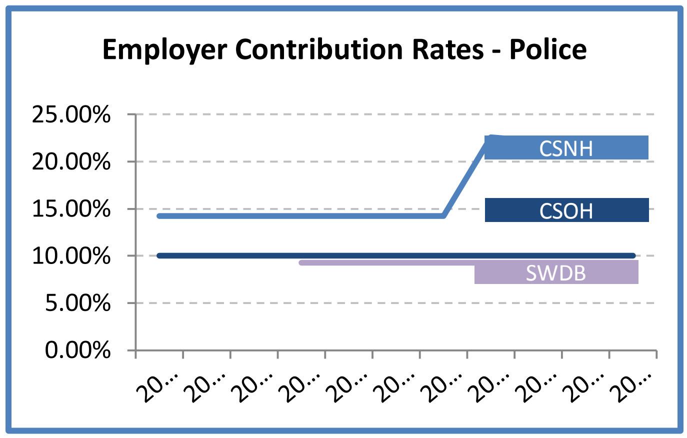
SWORN

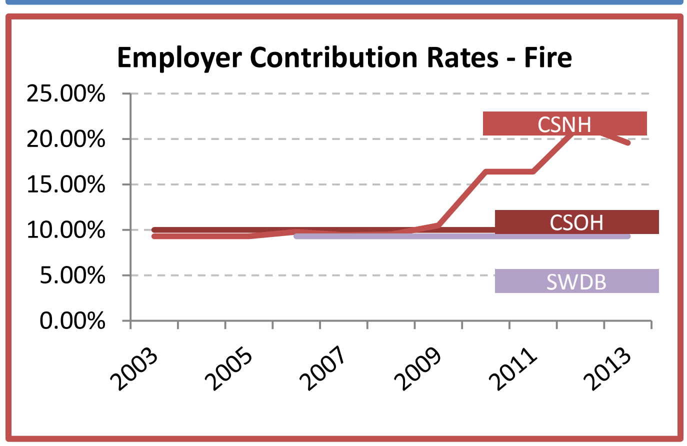
SWDB: State law requires the City and members to each contribute 8% of the members base salary to the plan. For those hired after January 1, 1997, the employee and employer must pay 1.3% for Death and Disability. In 2014, the plan members voted to increase their contribution amount by .5% per year for the next 8 years until the total contribution reaches 12% or 13.3%. At this time, there are no planned increases to the City's contribution.

CSNH: For both Police and Fire components, the plan requires the employer to make annual contributions in an amount sufficient to fund the plan in an actuarially sound manner. The employer contributions cannot be less than the employee contributions. In 2014, the City's contributions are 19.94% and 18.04% for Police and Fire, respectively plus 1.3% for Death and Disability for employees hired after January 1, 1997. In addition, the City was required to make lump sum payments to this plan in 2013 of $2,651,177. As of 2006, this plan was closed. All new sworn employees hired after this plan closed are enrolled in the Statewide Defined Benefit (SWDB) plan with greater plan flexibility and lower employer costs.

CSOH: City Council has the authority to establish and amend contribution rates in accordance with the actuarial analysis for this plan. Plan contributions are currently 10% for both the employee and employer. In 2013 years, the City made an additional annual lump sum payment of approximately $3 Million to this plan. As of 1978, this plan was closed to new participants.







The charts above related to CSNH and CSOH pension plans do not include data related to additional lump sum payments that have been made.

#2 – Are the City pension plans financially healthy?

- **Overall, we noted plans were considered healthy (fire and police plans) or improving in financial health (PERA) when we considered the reforms noted in this report.**
- **As of December 31, 2013, the funded ratio for fire and police plans exceeds the 80% funded ratio considered by actuaries as a key indicator of financial health, while the civilian plan (PERA) was funded at 73.1%.**
- **Although the City still has exposure to some of the indicators of troubled plans, we noted the exposure is less than the troubled plans in the national media identified in this report.**

We reviewed literature such as plan annual reports to identify key measures of financial health. These sources referenced three key indicators of financial health.

Three key indicators of financial health we considered were:

- **Funding Ratio**
- **Investment Rate of Return**
- **Amortization Period**

Financial Measure - FUNDING RATIO

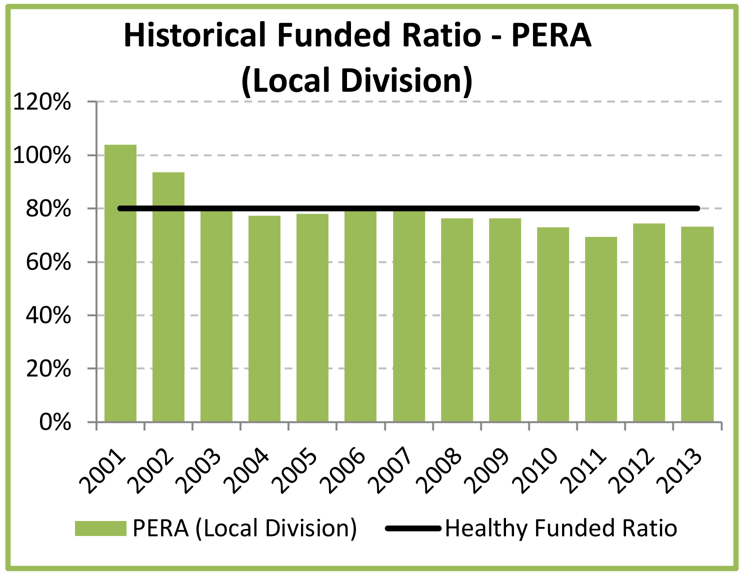
The first financial measure we reviewed is the funding ratio, which is the ratio of fund assets to the calculated future benefits. A common benchmark used by the American Academy of Actuaries is that plans should be at least 80% funded with a goal of 100%.

The funding ratio is a point in time measurement, and is calculated by the plan administrator using the actuarial value of future benefits based on stated assumptions and the current plan assets. The trend in the funding ratio is as important as the level at any point in time.

Funding ratio - PERA

The PERA plan's funding ratio has been less than 80% since 2008, falling as low as 69.3% in 2011. For several years prior to 2008 the plan maintained a ratio closer to 80% or higher, dipping as low as 77.2% in 2004. We noted the projected investment rate of return, discussed in the next section, has a significant impact on the funding ratio of a plan.

Beginning in 2004 and again in 2006, PERA employers were required to remit increased contributions from 10% to 13.7% in an attempt to improve financial health. These additional contributions may be discontinued when plan metrics are deemed healthy. It can be seen in the next chart that the PERA plan is not currently meeting the 80% funding ratio benchmark, however steps are being taken to improve financial health of the plan. See page 12 for information on recent PERA plan reforms.



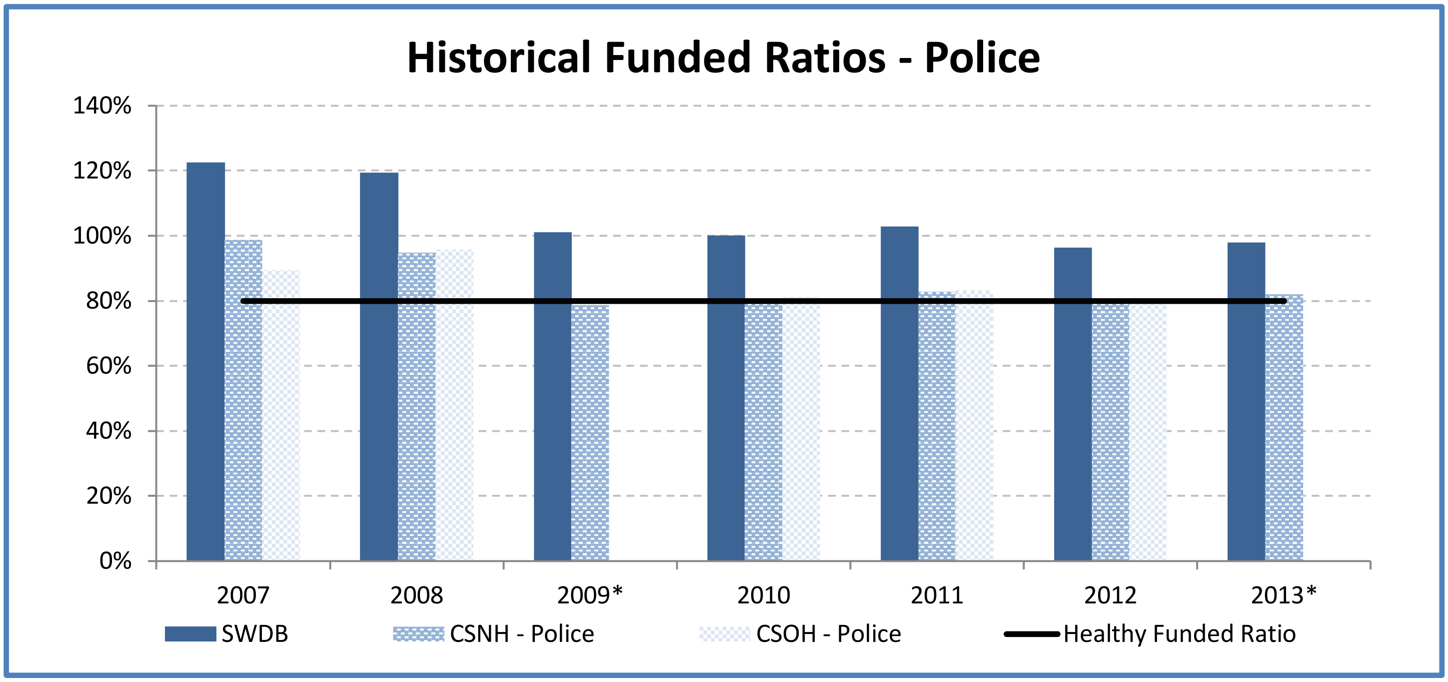
The funding ratio is impacted by assumptions related to investment returns. The chart above shows the funding ratio calculated by PERA based on the assumed rate of return, which has been reduced in recent years. In 2003, the assumed rate was reduced from 8.75% to 8.5%; in 2010 reduced to 8% and for 2013, the rate was again reduced to 7.5%. Per the sensitivity analysis included in PERA's 2013 Financial Report, the funding ratio would be 77.3% if the rate of return was still 8%. Similarly, if the rate of return was 9%, the funding ratio would be 85.9%. Actual rates of return earned by PERA can be seen on page 8 in this section.

The next chart illustrates the local government division funding compared to other PERA divisions.

PERA Division Funding Levels (12/31/13)	
Denver Public School	81.2%
Local Government	**73.1%**
Judicial	73.0%
School	60.3%
State	57.5%

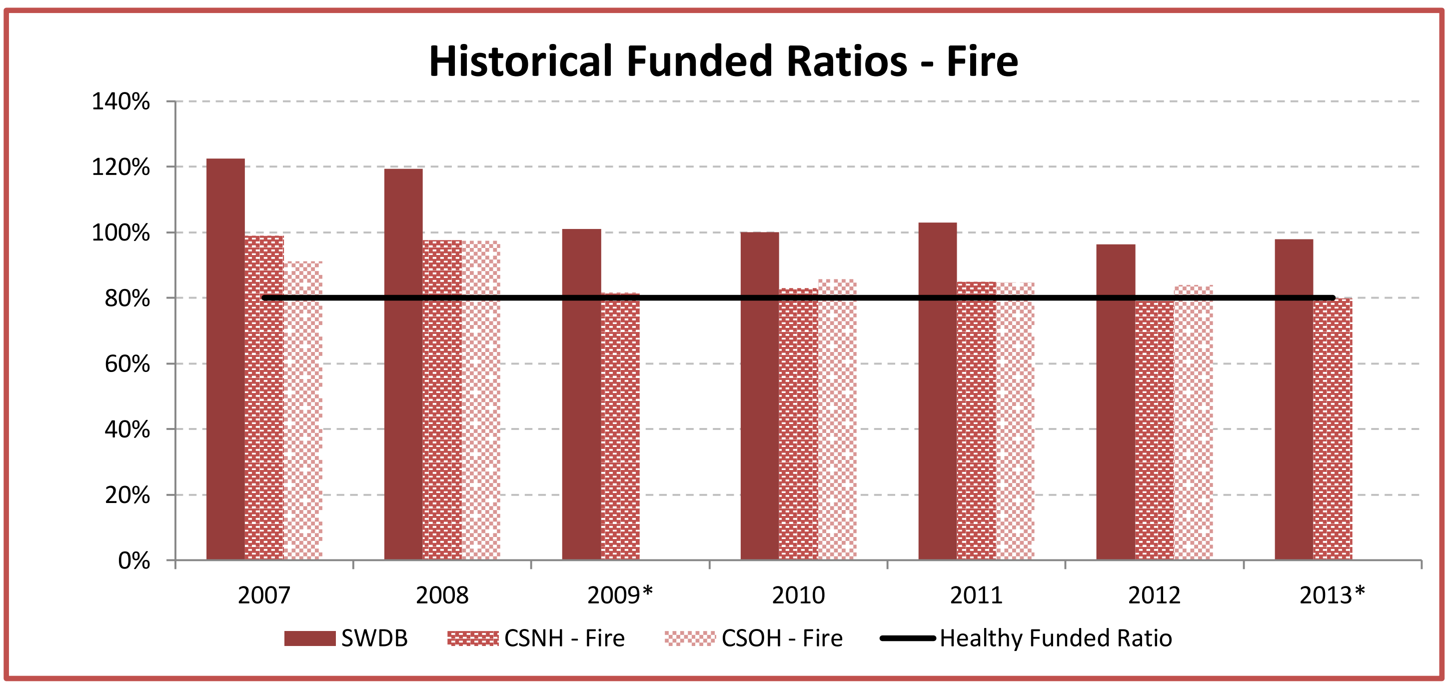
Funding ratio – Sworn

The sworn plans have consistently maintained a funding ratio of 80% of higher. Both the CSNH and CSOH plans require the City to increase contributions as needed to maintain funding status. The City made additional lump sum payments to those plans in recent years to maintain financial health. The SWDB has historically been the best funded sworn plan.



Source: Colorado Fire and Police Protective Association Annual Reports: FPPAco.org\pdfs\annual_audit_actuarial_reports for 2007 through 2013.

** CSOH data was not available for 2009 and 2013*



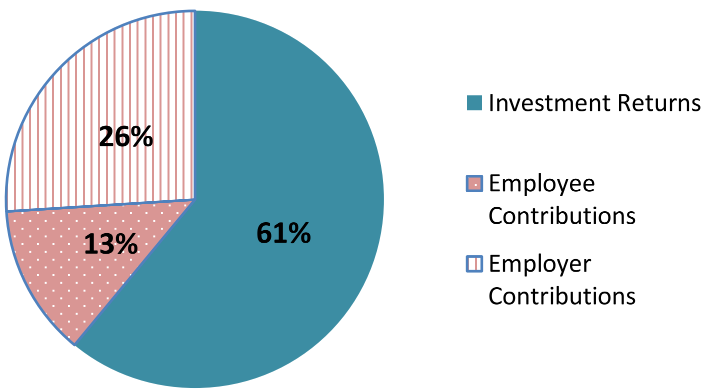
Source: Colorado Fire and Police Protective Association Annual Reports: FPPAco.org\pdfs\annual_audit_actuarial_reports for 2007 through 2013.

** CSOH data not available for 2009 and 2013*

Financial Measure - INVESTMENT RATE OF RETURN

The second financial measure we evaluated was the investment rate of return, which is the ratio of money gained or lost on an investment compared to the amount invested.

Public pension plans rely significantly on investment returns. Per the 2010 US Census Bureau Annual Survey of Public Pensions, investment returns typically make up over 61% of the pension sources of revenue, with the remainder consisting of employer and employee contributions.



Source: Public Pension Plan Funding per US Census Bureau

According to a study on public pension funding, the median interest rate used by plans decreased from 8% to 7.75% in 2013. All City pension plans assumed a 7.5% future investment return rate in 2013. If the assumed rate of return is higher than the actual return rates, the fund assets might be overstated and financial metrics could be deemed healthy when they are not. Similarly, failure to assume a realistic rate of return could create a situation where contribution rates are unnecessarily raised in order to increase the plans financial metrics to a specific goal.

Investment rate of return – PERA

PERA's actuarial, or assumed, rate of return was 8.5% beginning in 2003; in 2010 the actuarial rate of return was reduced to 8%. The PERA Board of Trustees elected to reduce the assumed rate of return to 7.5% effective for 2013 financial reporting.

Actual rate of return has been as high as positive 24.1% and as low as negative 26%, with an average rate of return of 7.6% over the last 10 years.

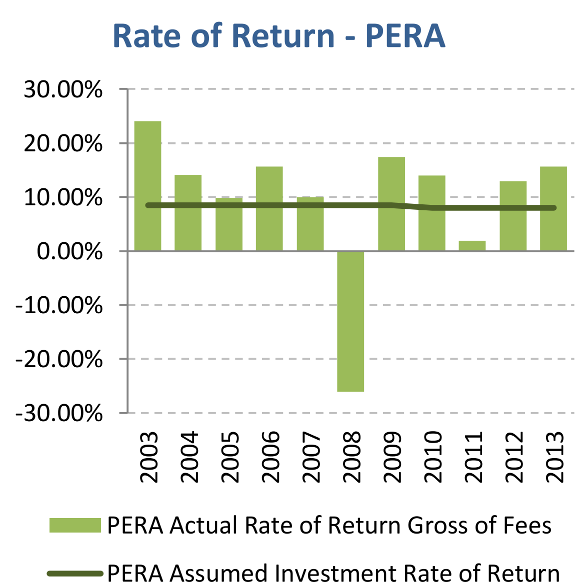
IMPORTANCE OF INVESTMENT RETURNS

Public pension plans rely significantly on investment returns

Lower rates of return over time will reduce a plan's ability to meet its obligations

If the assumed rate of return is higher than actual return rates, the fund may not be sufficient to meet its financial obligations. This creates a risk of increased contribution rates in the future to improve the financial health of the plans.

The Milliman 2013 Public Pension Funding Study found 29 of the 100 plans lowered their interest rate assumptions since the 2012 study. The median interest rate used by the plans decreased from 8.00% in the 2012 study to 7.75% in the 2013 study. This drop is in line with a declining market consensus on expected long-term investment returns. Lower interest rate assumptions cause accrued liabilities to increase and funded ratios to fall.

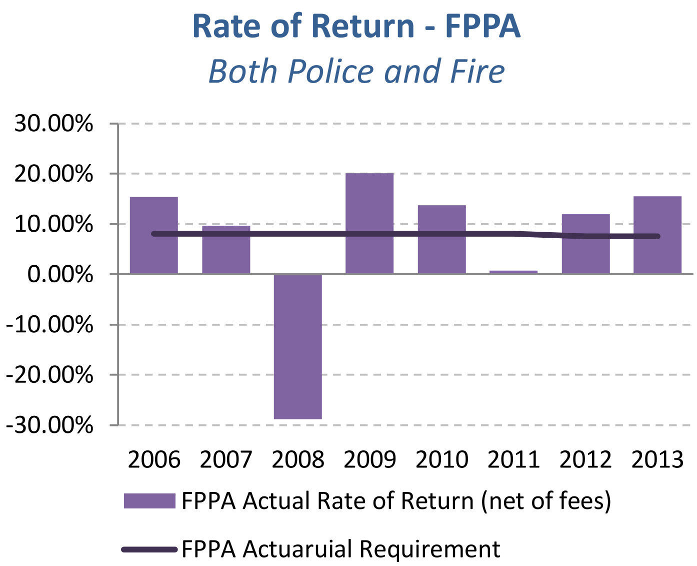


Investment rate of return – Sworn Plans

The sworn CSOH, CSNH and SWDB plan's actuarial rate of return was 8% prior to 2012 when it was reduced to 7.5%

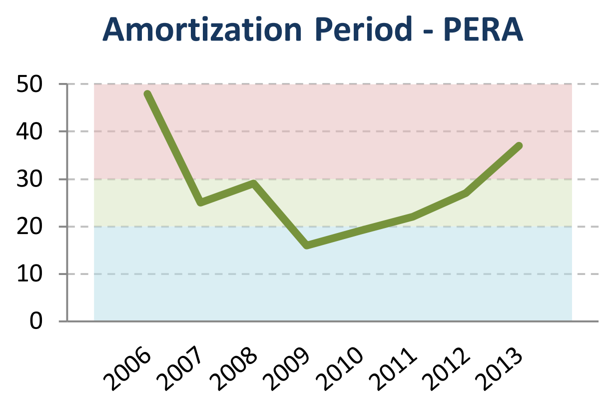
The actual FPPA plan returns showed a similar pattern of returns to the PERA plan.

Amortization Period	
Less than 20 years	Conservative
20 – 30 years	Healthy
31 - 39 years	Unhealthy
40 years or more	Unsound



Amortization period – PERA

The PERA fund amortization period was at a level considered healthy or better between 2007 and 2012. Changes in 2013 financial statements resulted in an amortization period of 37 years, which is considered unhealthy.



FPPA Actuarial Rate of Return

Actual market rate of return over the past 8 years has varied.

Past 3 years: 9.37%

Past 5 years: 12.37%

Past 8 years: 7.25%

*Only 8 years are shown because Colorado Springs joined the SWDB in 2006

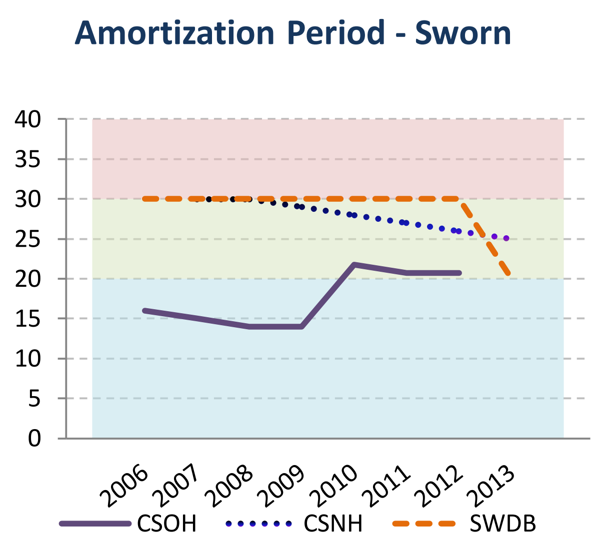
Amortization period – Sworn (CSOH, CSNH and SWDB)

All FPPA plans had amortization periods considered healthy for the years we reviewed, as seen in the chart.

Financial Measure – Amortization Period

The third and final financial measure we reviewed was the amortization period. The amortization period is the length of time required to eliminate a pension plan's unfunded liability based on current assumptions.

As of 2012, the Governmental Accounting Standards Board (GASB) recommends that public pension plans maintain an amortization period of not more than 30 years. A lower amortization period is considered better. The Pension Review Board considers plans with an amortization period of 40 years or more to be actuarially unsound.



FINANCIAL HEALTH - CONTINUED

Comparison to Troubled Plans

In recent years, the financial difficulties of some cities have been well publicized nationally. The cause of these difficulties included employees not contributing significantly to the plan, eligibility for retirement at a young age, ability to spike pension through ending salary, and excessive cost of living adjustments.

We identified common themes of troubled plans and compared these indicators to the public plans in which City of Colorado Springs employees participate.

Factor common in troubled plans	Is this factor present in the plans that City employees participate in?
Employees contribute little or nothing to the plan	No. Civilian employees are mandated by state law to contribute 8% toward their PERA retirement, and sworn employees are mandated by state law to contribute 8% to 10% toward their retirement. SWDB members recently elected to increase their contributions.
Employees can retire at a relatively young age with a high percentage of salary	Somewhat, for older plans, but it is improving. While retirement age can be lower than for private sector, it is older than some troubled plans. Under PERA, the employee must be at least 50 years old with 30 years of service to receive full benefits. For CSNH, the retirement age requirement is 50 for Police and 55 for Fire. For SWDB plan participants, normal pension starts at age 55 with 25 years of service. The requirements are increasing so the combined age and years of service will be 90 in the future. **In comparison:** Public safety workers in CalPERs, the California Public Pension program, can retire at age 50 after 30 years of work with benefits equal to 90 percent of their final salary. This level of benefits has put CalPERs in financial trouble.
Employees can 'spike' pay by getting big raises or working overtime in the final years of their job	Somewhat, compared to private plans, but this is improving. Legislative changes to PERA require an 8% per year 'spike cap' applicable to members eligible to retire after January 1, 2011. For CSNH and SWDB Fire participants, scheduled (required) overtime is part of the pension calculation, but additional overtime is not. For CSNH and SWDB Police participants, overtime is not part of the pension calculation.
Employees can retire, then be rehired and receive both salary and pension at the same time (double dipping)	Somewhat, employees who retire under PERA are limited to 110 days or 720 hours compensation in exchange for services without affecting retirement benefits. Effective January 1, 2011, all retirees working after retirement for a PERA employer, must pay a working retiree contribution. The contribution percentage applicable to working retirees is the same contribution percentage in effect for an active member who is working for that employer. The working retiree contributions do not accrue an additional benefit and retirees are not eligible for a refund of these contributions. Sometimes this is allowed for sworn employees. If a SWDB retiree returns to work for the same employer, the employee will not receive a pension payment while he/she is working for the former employer. However, the employee may receive a pension payment while working after retirement for an FPPA affiliated entity other than the former employer. **In comparison**: California, New Jersey, Utah, and other states, public workers can "retire" early and then either resume their existing job or take a new job, thus receiving a salary and pension at the same time.

The retirement benefits payable to plan participants are excessive because the employee can earn 100% of salary in retirement	Possible, but not likely based on 2013 retirements, the average PERA retiree was receiving 43% of ending salary. The average fire and police retiree was receiving 71-73%. • Current Plans - The length of service to obtain 100% benefits is currently 40 or more years for PERA retirees and 42 years for FPPA SWDB plan participants. • For the closed sworn plans with active participants: o CSNH Fire Plan - Allows a maximum benefit of 77% of base salary after 30 years of service and 55 years of age. o CSNH Police Plan - Allows a maximum of 75% of base salary after 30 years of service and 50 years of age.
The retirement benefits payable to plan participants are excessive because of costs related to Cost of Living Adjustments (COLA)	Somewhat, although this is improving because recent changes have placed limitations on the amount of the COLA. • COLA for PERA are limited to the lesser of the Consumer Price Index for Urban Wage Earners and Clerical Workers (CPI-W) or 2% • The SWDB plan COLA are limited to the COLA that can be paid by the plan and remain financially sustainable. • However, the CSNH plan allows COLA increases up to 3% subject to inflation limitations. However, COLAs may not start for up to 10 years after retirement at age 60 for Police or age 65 for Fire. **In comparison**: Illinois government retirees receive COLAs of 3% regardless of inflation. Per the Illinois Policy Institute special report dated November 2013, retirees experience rapidly increasing pensions due to the annual automatic 3% compounding COLAs.
Employer contributions are more than 50% of employee wages	No, in 2013 employer contributions for PERA were 13.7% of employee wages. For the sworn plans combined, the employer contribution rate with additional lump sum payments was an effective rate of 24% of sworn wages. **In comparison**: In the September 2010 Pension Sustainability Audit Report to City of San Jose City Council, the employer contributions for police and fire members was projected to be 69.9% of sworn payroll for 2013.

New Governmental Accounting Standards

New governmental accounting standards will require the City to include the City's share of unfunded pension liability from all pension plans on the December 31, 2015, financial statements. Governmental Accounting standards 67 and 68 will require more transparency related to future expected costs of pension plans.

#3 – What has been done to improve pension health?

- **Since 2006, all new sworn employees have been enrolled in the SWDB plan, which has lower costs and benefits as well as the governing board having authority to make plan changes other than employer contribution rates.**
- **City sworn employees participated in the task force that recommended members increase their contribution to the SWDB plan. Members will begin making additional contributions in 2015 until members are contributing 12% or 13.3%. City contributions will remain at 8 % or 9.3% depending on the employees start date.**
- **PERA plans have reduced the impact of cost of living adjustments, made adjustments to ending salary calculations, and increased age or service requirements to receive benefits.**

PERA Reforms

Senate Bill SB-1, passed by the State Legislature in 2010, introduced reforms to PERA to reduce retiree benefits.

Key changes were as follows:

- The annual maximum cost of living adjustment was reduced from 3.5% to 2%.
- Vesting match was increased to 5 years.
- Employees are required to contribute to the plan if they work for a PERA employer after retirement.
- The calculation of the 3-year Highest Average Salary (HAS) was changed to include a base year and an 8% spike cap for members eligible to retire after 1/1/11.
- Service Retirement Eligibility Rule of 80 will increase to 90, i.e., to receive full benefits, age plus years of service must equal 80, but will gradually increase to 90.

SWDB Plan Reforms

Fire and police – Effective in 2006, new fire and police employees enrolled in the SWDB plan, which had lower costs and benefits. Also, the SWDB governing board has authority to make plan changes other than increases to employer contribution to ensure plan financial health. The lower cost and flexibility under the SWDB plan were not possible in the closed CSOH and CSNH plans.

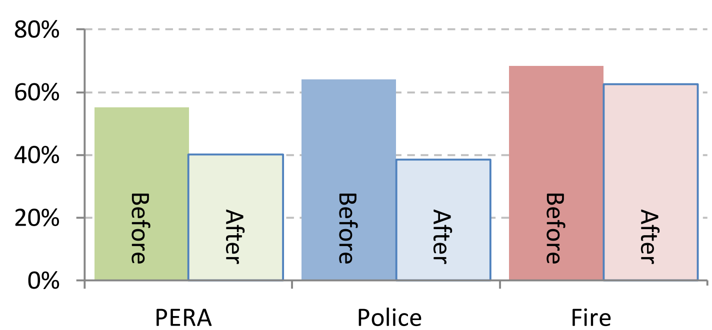
City fire and police employees participated in a task force that made a recommendation for members to increase their contributions. Members will begin contributing an additional .5% per year until member contributions reach 13.3%. Employer contributions will remain at 8% or 9.3% depending on hire date. Over time, the City's sworn workforce will participate in the SWDB plan in which the employer contribution is less than the employee's contribution.

Reforms that accompanied the adoption of the SWDB plan include:

- Cost of living adjustments are based on plan financial resources rather than on an index such as consumer price increases. Cost of living adjustments for the SWDB plan have been significantly lower than in the old plans (0.48% for 2012 vs. 2-2.5% for the CSNH plans).
- Final average salary calculations for the SWDB plan are based on the three years of highest annual salary (HAS), as compared to the last 18 months for the CSNH plan.
- The contribution rates for the SWDB plan are lower; with the employee and employer currently each responsible for 8% or 9.3% depending on hire date.
- The formula to receive full benefits (age plus years of service) requires the participant to be at least age 55 at retirement. This requirement was an increase for Police.
- Plan rules such as eligible retirement age and future benefits can be changed by the FPPA Board to ensure the plan remains financially sound.

In addition to the above reforms, sworn plan costs have also been managed by closing older plans and having new participants enroll in SWDB. While the short term cost of the closed CSOH and CSNH plans is high, the long term cost of the pensions will be decreased. This is an example of managing pension costs.

Benefits Received - Estimated Impact of Reforms and Plan Changes



Impact of new plans –To the left is 2013 retiree average benefit calculated by the auditor making different assumptions. To calculate "Before", the retirees were assumed to be on older plans (PERA before SB-1 and the CSNH plans for sworn employees) and their benefits do not reflect the recent pension reforms. The average benefit is shown as a percentage of average salary. For "After", the auditor estimated benefits assuming newer plans rules (PERA after SB-1 and the SWDB plan for sworn employees).

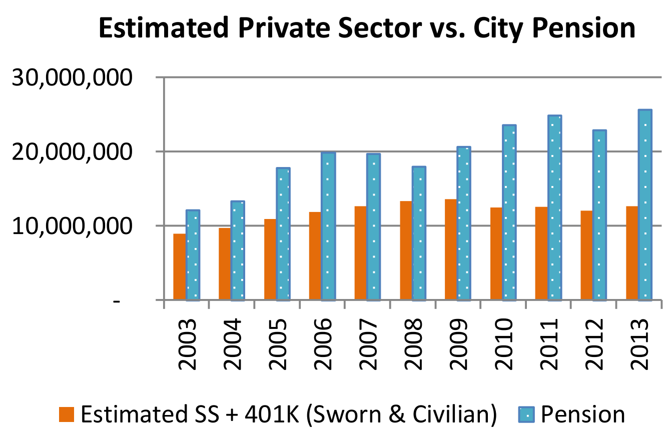
#4 – How do the City pensions compare to the private sector?

- **Employees receive a higher benefit through participation in City pension plans as compared to the private sector.**
- **The City pays more for pensions than would be required for Social Security in the private sector.**
- **Based on 2013 retirements, police and fire retirees had more years of service as well as higher ending salaries, and would qualify for a higher retirement benefit than civilian retirees.**

Additional Cost of Pensions

To calculate the estimated additional cost for the City plans, we utilized retirement data per City Finance for all employees who retired in 2013. To compare the costs of pensions to private plans, we calculated the employer contributions to Social Security, as well as an assumption of a 401(k) retirement matching contribution of 3%. We conclude there was an additional cost to provide a public pension plan over a typical private sector plans as noted in the following chart.

For 2013, we estimated the additional cost to the City to provide pensions for civilian and sworn employees combined was approximately $13 million.



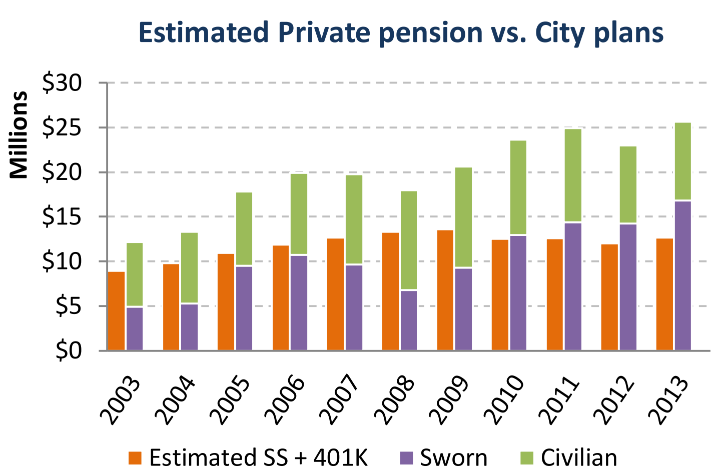
Source: Employer pension contribution amounts per City Finance. This graph includes City Enterprise Funds except Colorado Springs Utilities and Memorial Health Systems. The Pension number above includes 1.02% for post-employment healthcare.

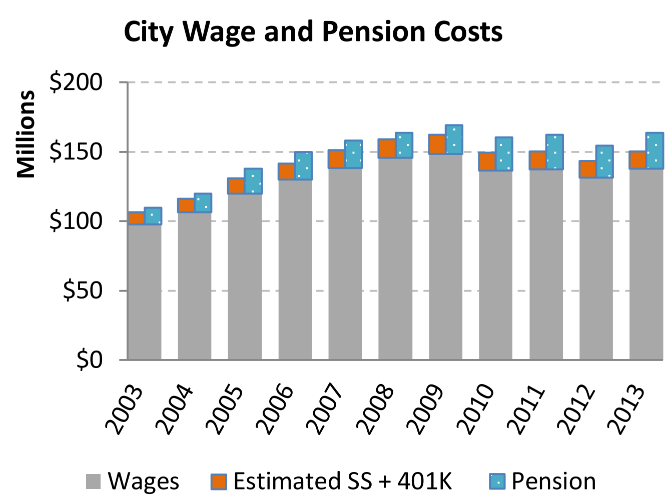
Calculation Assumptions

If under the Social Security system with a typical defined contribution plan (such as 401k or 403b), presume both employer and employee contribute required payments to Social Security. Additionally, presume that employee and employer make contributions of 3% each to a defined contribution plan.

Information is based on actual wages obtained from City Finance for each year.

Of the total pension costs in 2013, approximately $8.9 million related to civilian employees, while $16.8 million relates to sworn police and fire plans.

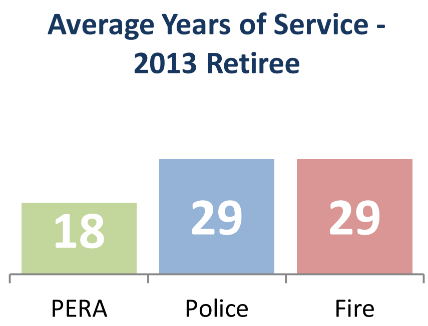


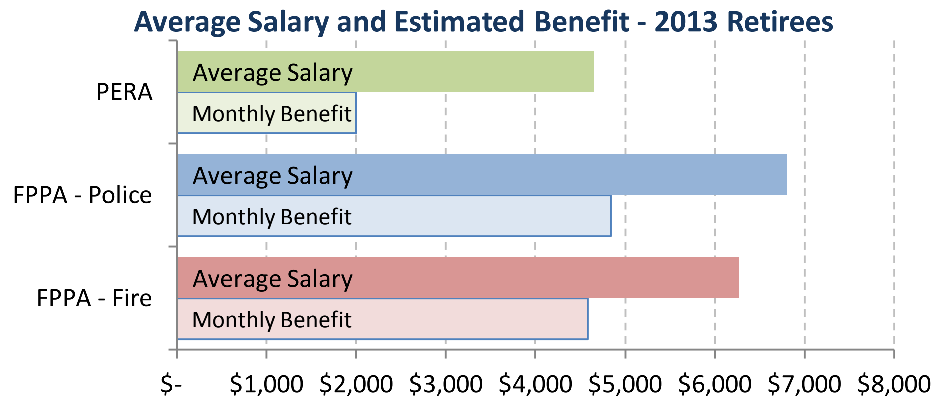


Source: Employer pension contribution amounts per City Finance. This graph includes City Enterprise Funds except Colorado Springs Utilities and Memorial Health Systems.

Average salary and benefit for 2013 retirees

Based on 2013 retiree data obtained from City Finance, we noted that police and fire (sworn) retirees had significantly longer length of service and higher ending salaries. Over the ten year range the average PERA retiree had 22 years of service and the sworn retirees had 27 years of service reflecting lower average final salary for PERA employees and higher for sworn employees. The City is only aware of actual years of service worked for the City. PERA members can buy years of service or accumulate years of service at other PERA employers, which have not been considered.





For the 2013 average retiree from each plan, the estimated private retirement plan benefit as compared to the public pension benefit plan was calculated. Since PERA retirees had fewer years of service on average, the estimated benefit was closer to the private sector benefit. Length of service is a significant factor in the monthly benefit calculation. See the chart on page 12, which illustrates the effect on monthly benefit of recent reforms.

Key Assumptions – Average Benefit

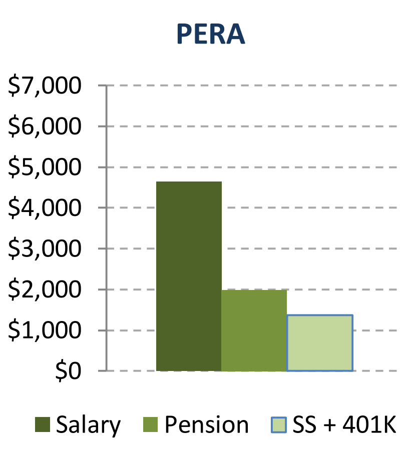
Estimated benefit was calculated using 2013 average final salary and years of service for each employee group per City Finance. A Social Security calculator was used to estimate prior salary. The Social Security calculator was utilized because annual salary data prior to 1999 was not available.

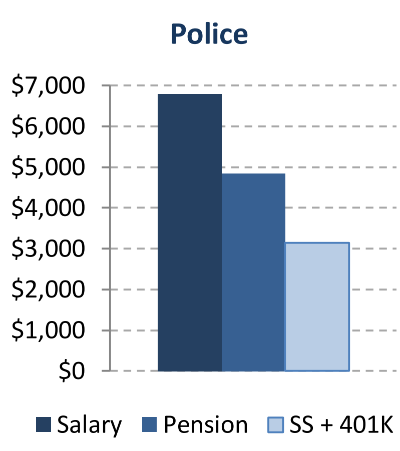
We note that the assumed rate of return for the 401(k) plan was 7.5%, consistent with the PERA rate of return assumption. Actual rates of return depend on individual returns and investment choices.

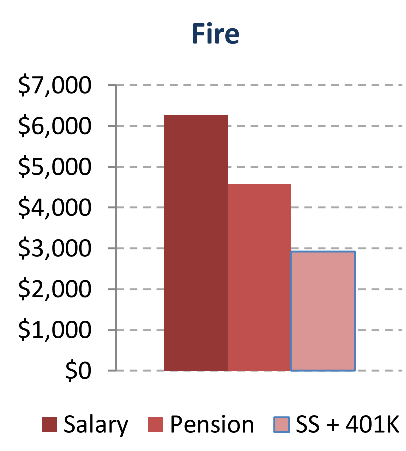
The Social Security benefit was calculated using the assumption that the employee retired at age 62 which was considered closer to typical City employee's retirement age.

Pensions were calculated under the CSNH plan for sworn employees. For PERA employees, we assumed the retirees began employment prior to 2005.

Estimated average monthly 2013 retiree pensions







#5 – What is the total cost of pensions paid by the City?

- **Total pension costs paid by the City in 2013 were $25.7 million.**
- **Total employer pension costs have increased 111% or average of 10% per year since 2003 for all plans combined.**
- **Much of the increase was related to the CSOH and CSNH pension plans which are closed to new entrants.**

In 2003, PERA represented 60% of the total pension costs while the sworn plans represented 40%. Over the past 10 years this ratio has more than reversed. In 2013, PERA represented 34% of pension costs while sworn have increased to 66%. Since 2003, civilian employees have decreased by 23% and sworn employees have increased by 27%.

As of December 31, 2013, there were 1,107 active employees enrolled in sworn plans, and 1,325 active employees enrolled in the civilian plan. The total number of active employees enrolled in sworn plans has increased by 27% since 2003, while the number of active employees enrolled in PERA decreased by 23% over the same period.

Civilian Pension Costs

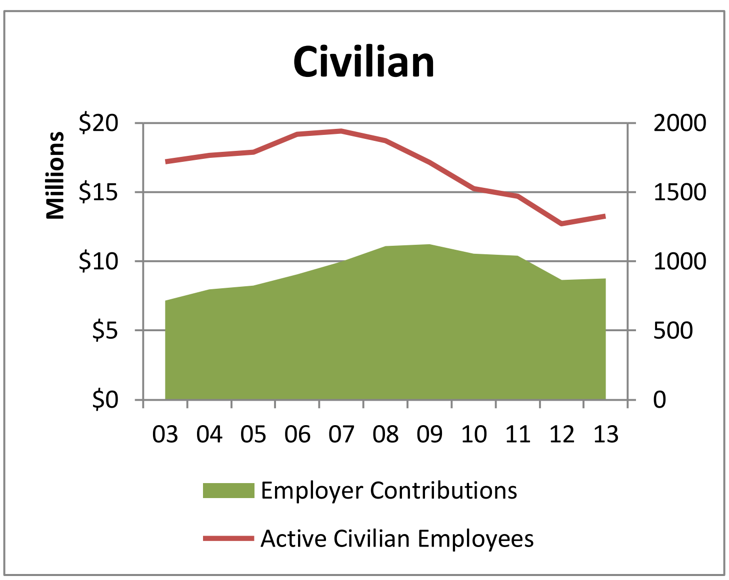
In 2013, the City paid $8.9 million in pension contributions to PERA, which is a 22% increase over the 2003 payment of $7.3 million.

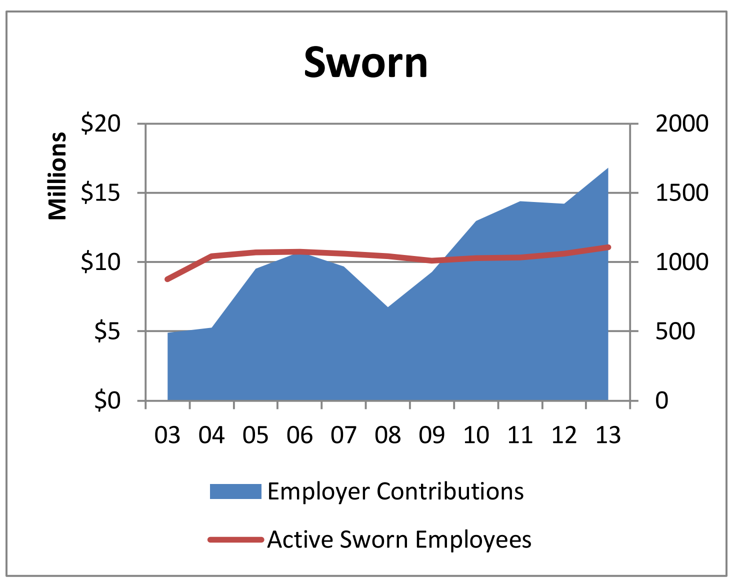
Sworn Pension Costs

In 2013, the City paid $16.8 million in pension contributions to the three sworn pension plans, which is a 243% increase over the 2003 contribution when including lump sum payments made to maintain financial health.

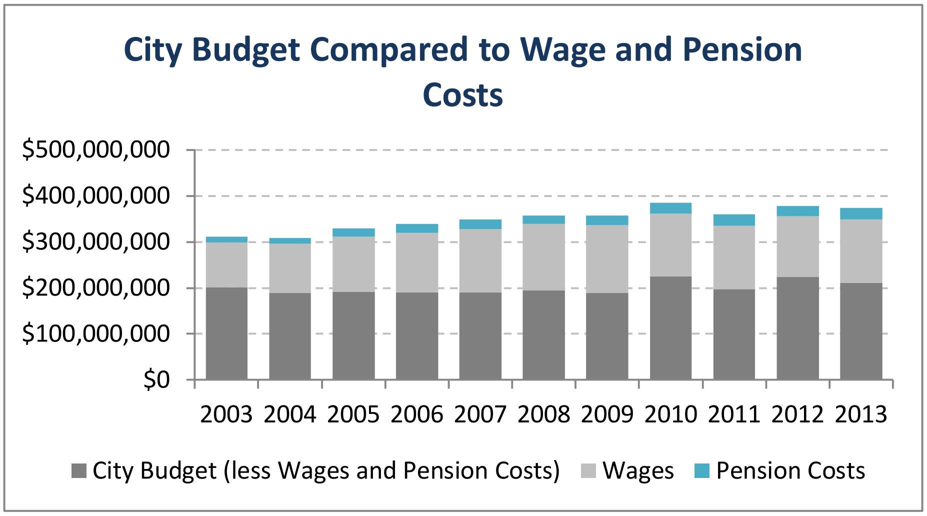
CSOH plan, which closed to new employees in 1978, has one active employee. 43% of fire and 66% of police employees participate in the CSNH plan, which closed in 2006 to new entrants. All remaining active employees are in the SWDB plan. The SWDB plan has an employer contribution rate of 8% or 9.3% depending on hire date and greater plan flexibility to maintain plan health than the other two plans. The City's 2013 cost for the SWDB plan was $2.1 million.

The CSOH and CSNH plans have had higher contribution rates and have required additional lump sum payments in recent years to maintain plan health. In 2013, the City paid $14.6 million to CSOH and CSNH plans combined. Closing the higher cost CSOH and CSNH plans should provide significant savings to the City in the future when most sworn employees will be in the SWDB plan.





Employer contributions per City Finance include City Enterprise employees, but exclude Colorado Springs Utilities and Memorial Health System.



In 2008, the City did not make a contribution to the CSOH plan which accounts for a portion of the decline in contributions that year. Also, amounts above do not include City's additional lump sum payments made in recent years.

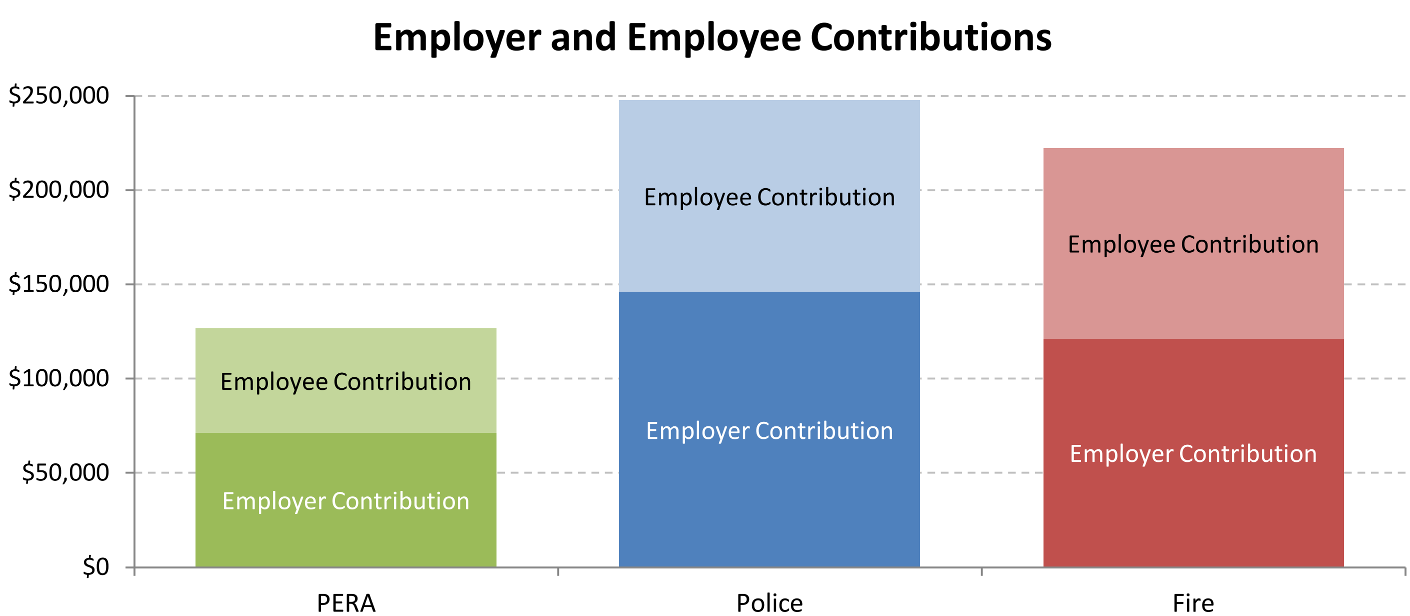
PENSION COST - CONTINUED

Since 2003, the City Budget (all funds) has increased approximately $62.7 million or 20%. During this same period employer pension costs have increased approximately $13.5 million which is a 111% increase. In 2003, pension costs represented 3.9% of the total all funds budget. In 2013, pension costs were 6.8% of the budget.

Employee Pension Contributions

The average employee contributed over 40% of the cost of their retirement benefit for all plans as indicated in the charts below.

Employee VS Employer Contributions over the Average Years of Service for the 2013 Retiree



Auditor calculated using 2013 average ending salaries. Social Security calculator was used to determine previous year's salaries. The effective Social Security and pension rates were applied to the estimated salaries per the contribution amounts. Contributions do not include the health care trust fund for PERA (1.02%) employees and does not include the death and disability contribution (1.3%) for sworn employees. The graph does not include lump sum contributions made by the City to closed sworn plans.

City Council's
Office Of The City Auditor

About our Office
The mission of the Office of the City Auditor is to provide City Council with an independent, objective and comprehensive auditing program for operations of the City. Our auditing program includes:

- Evaluating the adequacy of financial controls, records and operations
- Evaluating the effectiveness and efficiency of organizational operations
- Providing Council, management and employees objective analysis, appraisals, and recommendations for improving systems and activities

The Office of the City Auditor is responsible for auditing the systems used by the City of Colorado Springs and its enterprises, including Colorado Springs Utilities. We perform a variety of audits for these entities, including financial audits, performance audits, contract audits, construction audits, and information system audits. We also perform follow-up on a periodic basis to monitor and ensure management actions have been effectively implemented.

Authorization and Organizational Placement
Our audits are conducted under the authority of Chapter 1, Article 2, Part 7 of the Colorado Springs City Code, and more specifically parts 703, 705 and 706 of the Code. The Office of the City Auditor is structured in a manner to provide organizational independence from the entities it audits. This independence is accomplished by the City Auditor being appointed by and reporting directly to the City Council.

Audit Standards
The audit was conducted in a manner that conforms with the International Standards for the Professional Practice of Internal Auditing, a part of the Professional Practices Framework promulgated by the Institute of Internal Auditors.

The audit included interviews with appropriate personnel and such tests of records and other supporting documentation as deemed necessary in the circumstances. We reviewed the internal control structure and compliance tests. Sufficient competent evidential matter was gathered to support our conclusions.

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