



Workforce Development

Relieving the Tension with the Pension:
An Analysis of the El Paso Fire and Police Pension Underfunding

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Executive Summary

The El Paso Fire and Police Pension Fund's ability to provide adequate retirement benefits to its members has recently been questioned due to a current \$365 million underfunding. To understand more about the issue, Community Scholars decided to look into the pension fund's current structure, past and present proposals to resolve the situation, and problematic and successful plans outside the El Paso Del Norte region that could provide a point of comparison for the El Paso Fire and Police Pension Fund.

El Paso Firemen and Policemen's Pension Fund (EPFPPF)

According to Jake Soteriou, Ex-Chairman of the EPFPPF, the primary cause for the underfunding in the pension fund was the past use of outdated mortality tables. A mortality table is a set of statistics that is used to predict the life-expectancy of a member, and thus the amount of money each will retrieve throughout the course of their retirement.¹ Basically the problem was that members were generally living longer than was predicted by the tables and were thus receiving more money from the pension fund than originally predicted. Another factor that contributed to the underfunding was the automatic 3% cost of living adjustments, or COLA, which increases a retiree's monthly pension annually to account for inflation and the rising price of goods and services. COLA is thought to be problematic because it increases the pensions at a rate which surpasses inflation; consequently giving the retirees more money than is necessary.² Finally, part of the reason why the underfunding problem has worsened to its current state is due to a lack of attention by local politicians when the problem first began to arise. If appropriate actions were taken when the problem first originated, the problem would not have reached its current state.³

The proposed solutions for the underfunding problem in the EPFPPF involve the sale of pension obligation bonds by the city, a raise in member contribution rates, and the creation of a second-tier benefit plan for future members. As for the obligation bonds, the city will hold two sales. The first took place already in July 2007 and was valued at \$100 million. The second will be held in July 2009 and will value \$110 million.⁴ The member contribution rates were increased by 2%, meaning that firemen are now required to contribute 15.28% of their paychecks, while policemen contribute 13.89% to the fund. Lastly, under the second-tier plan, future members will be required to contribute a larger amount of their paychecks to the pension fund. In order for future members to qualify for normal retirement, they must work for 25 years instead of 20. Also, the retirement age was increased from 45 years to 50.⁵ In terms of a timetable, an actuarial valuation of the fund, conducted by Buck Consultants, revealed that with these revisions in place it will take 40 years to resolve the underfunding problem and obtain a 90% funded status.⁶

¹ El Paso Firemen and Policemen's Pension Fund. "City of El Paso Firemen and Policemen's Pension Fund." El Paso Firemen and Policemen's Pension Fund. 12 June 2007. <<http://www.elpasofireandpolice.org/PlanDoc.pdf> >.

² Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

³ Feidner, Robert. Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

⁴ Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

⁵ El Paso Firemen and Policemen's Pension Fund. "City of El Paso Firemen and Policemen's Pension Fund." El Paso Firemen and Policemen's Pension Fund. 12 June 2007. <<http://www.elpasofireandpolice.org/PlanDoc.pdf> >.

⁶ Buck Consultants. El Paso Firemen's Pension Fund: Actuarial Valuation. 1 January 2004. Buck Consultants. 12 June 2007. Dallas, TX.

El Paso City Employees Pension Fund (EPCEPF)

Similar to the El Paso Fire and Police Pension Fund, the El Paso City Employees Pension Fund (EPCEPF) is also encountering underfunding problems. Though not as drastic, the EPCEPF underfunding is totaled at \$103 million.⁷ The causes for the underfunding in the EPCEPF, as described in an actuarial valuation of the fund completed by Buck Consultants, are the use of inadequate contribution rates and longer life-expectancy for the members. From our research, Community Scholars discovered that the contribution rates for the EPCEPF members had not been increased in 20 years, which means that they have not kept up with inflation or the rising costs of services. Furthermore, the city pension fund relies on the stock market like the EPFPPF, and a stock market slump from 2000 to 2001 reduced the amount of money generated by the fund. To resolve these problems, the EPCEPF member contributions were recently increased by 1%, now requiring members to contribute 7.75% of their paycheck to the pension fund. Moreover, the city's contribution to the EPCEPF was increased by 1.4%. Now the fund is currently 84% funded, and with these revisions, is expected to obtain a 100% funded status by 2012.⁸

After completing our research and analyzing the data we obtained, Community Scholars developed the following conclusions and recommendations.

Conclusions

- 1. The underfunding problem in the El Paso Firemen and Policemen's Pension Fund arose in the 1960's, though it wasn't addressed until recently.** In years past, the underfunding was less than it is today. The problem would have been easier to resolve at that time with improved communication and further political courage.
- 2. If the underfunding continues to increase, it will eventually reach \$650 million in 10 years.** Chief of Police, Richard Wiles was quoted in a KVIA interview as saying that the underfunding grows at a rate of \$76,000 every day. This shows the importance of addressing the problem before the total exceeds half a billion dollars and nearly twice the city's annual budget.
- 3. The funding period to resolve the \$365 million fire and police pension underfunding problem is 40 years.** An actuarial evaluation of the fund completed by Buck Consultants revealed that it will take 40 years with revisions to resolve the problem and obtain a 90% funded status.
- 4. Because the plan is defined-benefit, a retiree's pension doesn't rely on the performance of investments in the stock market.** A member's retirement pension is based on the number of credited service years attained and his or her final wages. The investments the Pension Fund makes in the stock market, and the interest earned from these investments do not directly affect the members' retirement pension.
- 5. Police officers contribute less to the fund than firemen.** From our research, we have discovered that firemen are required to contribute 2% more of their salaries to the fund than policemen. The reason for this difference in contribution rates is that there are a higher number of policemen in the workforce than firemen.
- 6. The increase in property tax as a result of the City's contribution to the fire and police pension fund will be minimal.** Deputy City Manager, William Studer, stated

⁷ Sandoval, Juan F. Chairman: El Paso City Employees Pension Fund. Personal Interview. 21 June 2007.

⁸ El Paso City Employees' Pension Fund. "Non Uniformed Pension Contributions Proposed to Increase." 2007. [El Paso City Employees' Pension Fund](http://www.eppension.org). July 2007. <www.eppension.org>.

that the city's property tax will be increased by a minimal amount of 2%. According to him, this will only be a small effect on taxpayers.

- 7. The El Paso City Employees Pension Fund is expected to be fully funded in five years.** During a personal interview with Juan F. Sandoval, Chairman for the El Paso City Employees Pension Fund, he stated that by increasing member contribution rates the fund will achieve 100% funded status in five years.

Recommendations

Based on the research and the conclusions, Community Scholars recommends the following actions be taken in regard to the EPFPP.

- 1. All Board of Trustees members should be well informed in the areas of finance and investment.** According to Houston City Mayor, Bill White, being unaware of proper investment strategies leads to poor returns and an increase in underfunding. In order to prevent this from happening to the El Paso Fire and Police Pension Fund, Board of Trustees members need to become more aware of proper investments and accurate financing.
- 2. The Fire and Police departments should increase information and incentive to care to employees concerning the El Paso Fire and Police Pension Fund.** All employees and members of the fund need to be completely informed on the fund's status, as well as care about the complications the fund may be experiencing at any given time.
- 3. In the event of another under-funding issue in the future, authorities should address the problem immediately in order to prevent increased complications.** According to Deputy City Manager, William Studer, if the financial problems had been addressed in the past, there would not be a \$365 million underfunded amount now forcing the EPFPPF to increase contributions and cut benefits. Instead of pushing the problems back year after year, there needs to be resolutions immediately.
- 4. When developing a method to fix an underfunding situation, always consider what can be done in case the problem is not solved or other problems arise.** According to vice-chair of the EPFPPF, Michael Calderazzo, if this new plan fails, there is no alternate plan. Community Scholars believes that there should be multiple plans as backup in the case of unforeseen incidents.
- 5. Information that appears on the web site should be routinely updated and accurate so as to provide both department members and the general public with sufficient and adequate information.** The El Paso Fire and Police Pension Fund website should not have a disclaimer that makes no warranties for the accuracy timeliness, completeness, usefulness, or adequacy of the information provided.
- 6. The City of El Paso and the El Paso Firemen and Policemen's Pension Fund should maintain proper communication with each other and the community in order to prevent the issues of the past and present occurring again in the future.** Communication is the key to have a well-rounded system to insure that problems will not re-occur due to negligence or miscommunication from either party. Cooperation can assist in minimizing problems that may occur or develop into a crisis.

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According to the United States Department of Labor, a pension plan is an employee benefit plan established and maintained by an employer or by an employee organization, such as a union, that provides retirement income after the workplace.⁹ A pension plan could be the only source of income to a family or retiree after the conclusion of his or her employment and it is therefore important that the pension fund performs properly and provides adequate benefits to its employees.

The current pension plan that provides benefits for the El Paso Fire and Police Departments' retirees has recently been re-formulated by the El Paso Fire and Police Pension Fund Board of Trustees, City Officials, and financial advisors. This was done in order to save the fund from imminent insolvency, or lack of funds, in upcoming years. Even though the present plan adequately provides benefits for the current retirees, calculations show that in proceeding decades the plan will not be able to meet the growing number of retirees.¹⁰ For this reason, the fund has been labeled as *underfunded*, meaning that it fails to meet projections for future funding needs.

The El Paso Fire and Police Pension Fund (EPFPPF) is \$365 million underfunded.¹¹ In other words, if the city were to go out of business, the fund would be \$365 million short of paying the retirees their earned benefits.¹² To combat these funding challenges, the administrators of the fund have proposed several solutions. These include increasing the retirement age from 45 to 50, lengthening the minimum service years necessary to receive retirement benefits from 20 to 25 years, and raising their individual contributions by two percent. There is also a proposed property tax increase to occur over the next 30 years as well as pension obligation bond sales which will be detailed later in this paper.¹³ Raising the retirement age and expanding the minimum service years will lengthen the time in which employees will contribute to the fund as well as reducing the time they receive benefits. This, along with the two percent increase in contributions, will allow for more money to enter the fund.

To provide a basic foundation for what pensions are and issues associated with them, Community Scholars first looked at the nation's most common pension plan, Social Security.

Social Security

After the stock market crash in 1929, which sparked the Great Depression of the 1930's, the economy of the United States was in an economic crisis. The idea of "social insurance" was beginning to grow in popularity with the people of the United States. These new ideas grew into different organizations with goals to ensure the future economic safety of the American people. The "Share Our Wealth" program was one of the earliest organizations and was founded by Huey Long, the Governor of Louisiana from 1928 to 1932.

The Townsend Movement was another program that emerged from nation's economic insecurities. In 1933 Francis E. Townsend developed the Townsend Old-Age Revolving Pension Plan, better known as the *Townsend Plan*, after he found himself unemployed at age 66, with no savings due to the stock market crash. Coincidentally, this was the same year the

⁹ U.S. Department of Labor. "Retirement Plans. Benefits & Savings." U.S. Department of Labor. 4 June 2007. <<http://www.dol.gov/dol/topic/retirement/index.htm>>.

¹⁰ Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

¹¹ KVIA.com. "City looks to fix Pd and FD pension fund Tax payers could be Hit." KVIA.com. March 2007. 1 June 2007. <<http://www.kvia.com/global/story.asp?s=6076836&ClientType=Printable>>.

¹² Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

¹³ El Paso Firemen and Policemen's Pension Fund. "Summary Plan Description: Fire." 2007. El Paso Firemen and Policemen's Pension Fund. July 2007. <<http://elpasofireandpolice.org/spdfire.pdf>>.

EPFPPF had its first meeting to discuss their employee's pension. The idea behind his plan was for the government to give a pension of \$200 a month to every citizen over the age of 60. Part of this money would come from 2% of the nation's sales tax. At the time \$200 was a significant amount of money and to receive this pension an individual had to be retired, have no criminal record, and had to be able to spend money within 30 days. By 1935 there were more than two million members working to establish the Townsend Plan as the nation's pension system. The Townsend Plan even had continued support during the creation of President Franklin D. Roosevelt's Social Security Act of 1935 when most other alternate pension programs vanished. In 1949, 179 members of the House of Representatives forced a floor vote on the Townsend Plan, where it fell 39 votes short of replacing the Social Security system.¹⁴

Social Security Structure

Social Security is the general term for a public program that provides income and services to individuals in the event of retirement, sickness, disability, death, or unemployment. This social insurance uses contributions made by civilian workers and employers through taxes to provide income to people and their families in times of need. The employees under the EPFPPF do not contribute to nor receive benefits from Social Security, as they are not civilian employees.¹⁵

Social Security is funded through taxes, typically 8% of employee's earnings. For self-employed individuals, contributions are roughly 16% of their earnings. There are three deductions typically taken from a paycheck: one that funds Social Security's survivorship and retirement benefits, another which funds disability programs, and one that funds Medicare. Medicare is the country's health insurance program for people over the age of 65.¹⁶ These three deductions are put together as one tax from an individual's paycheck, which is in accordance with the Federal Insurance Contributions Act (FICA). FICA is the federal act which allows for the government to tax an individual's paycheck to provide national insurance.¹⁷ The deductions vary depending on an individual's annual income.

The largest benefit the FICA tax pays for is survivorship and retirement benefits. This tax is put into the Old-Age and Survivors Insurance (OASI) trust fund which is what provides the monthly benefits for people qualified to receive them. Another portion of this tax is put into the Disability Insurance (DI) trust fund, which provides disability benefits for employees with long term or mental disability.¹⁸

Problems with Social Security

Social Security is facing financial problems because of the growing number of retirees from the baby boomer generation. *Baby boomer* refers to people born during the sudden population boom following the close of World War II. With people generally living longer, the baby boomer generation retiring, and lower birth rates, the ratio of employee to retirees will change drastically. In fact, it is predicted that in about 10 years, there will only be two working employees for every Social Security retiree. Because of this insufficient ratio the Social Security System will start to pay benefits more rapidly than funds are received, depleting Social Security by the year 2041. This problem will affect the young population entering the workforce because

¹⁴ Social Security Administration. "Social Security: Medicare." January 2006. Social Security Online. 6 July 2007. <<http://www.ssa.gov/>>.

¹⁵ Calderazzo, Michael. Vice-Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 12 June 2007.

¹⁶ Social Security Administration. "Social Security: Medicare." January 2006. Social Security Online. 6 July 2007. <<http://www.ssa.gov/>>.

¹⁷ Social Security Administration.

¹⁸ John, David C. "How Today's Social Security Works." 2 March 2005. The Heritage Foundation. 26 June 2007. <<http://www.heritage.org/Research/SocialSecurity/bg1827.cfm>>.

the burden of funding the large number of retirees will be placed on them in the form of increased income taxation.¹⁹

This shift in demographics is not isolated to Social Security and is in fact having an effect on pension systems around the nation, including El Paso.²⁰ The following sections will discuss the El Paso firemen and policemen pension funds as well as the City of El Paso's pension fund.

The Current Police and the Fire Department Pension Plan

The Police and the Fire Departments' current pension plans are very similar and are categorized as defined benefit plans meaning that their employee benefits are based on a formula, using factors such as salary history and years of employment. Certain changes to the individual fire and police department's plans have been instituted to better fit each fund's employees' work tendencies. For example, police officers have a higher turnover rate than fire fighters and that is taken into consideration when formulating the plans.²¹ Currently, the fire fighters contribute 15% and the policemen contribute 12% to the fund.²² According to Michael Calderazzo, Vice-Chairman of the Board of Trustees of the EPFPPF these are among the highest contributions paid by public employees in the United States.²³

The reason policemen contribute less to the pension fund than a fireman is that there are more police officers employed at any given time than firemen. Furthermore, policemen average more overtime than firemen.²⁴ This affects the funding because though the employees contribute a percentage of their overtime pay, these contributions don't go to an individual's personal pension, but rather the general pension fund. Because of this, the fund's overall revenue is increased. Thus, the police department contributes a lower percentage of their paycheck because, as a group, they contribute more to the fund.²⁵ In general, the factors that determine how much is contributed to pension plan include an individual's salary, incentives or bonuses, length of active service, and overtime pay.²⁶

Moreover, the city is also required to contribute 18% of payroll each year to the pension fund.²⁷ This is the maximum amount the city can contribute to the fund under the current city charter.²⁸ This cap on city contributions has forced the city to search for alternate ways to increase the funding of the EPFPPF. Such alternate plans include the sale of obligation bonds, which will be detailed later in the report.

There have been recent revisions to the pension plans that affect the requirements for retirement, but not the main categories of benefits. The following sections will discuss some of the main benefit categories as they pertain to the El Paso Fire and Police Pension Fund.

Normal Retirement

¹⁹ Newyorklife.com. "Underfunded Pensions: The Next Threat to Retirement?" 2007. New York Life. 18 July 2007. <www.newyorklife.com/cda/0.3254.12362.00.html>.

²⁰ Newyorklife.com.

²¹ Calderazzo, Michael. Vice-Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 12 June 2007.

²² El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan." 5 March 2002. El Paso Fire and Police Pension Fund. June 2007. <<http://www.elpasofireandpolice.org/release.htm>>.

²³ Calderazzo, Michael. Vice-Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 12 June 2007.

²⁴ Calderazzo, Michael.

²⁵ Calderazzo, Michael.

²⁶ El Paso Police Department. "Summary of Pay and Benefits." 2007. El Paso Police Department. June 2007. <http://www.ci.el-paso.tx.us/police/salary_benefits.asp>.

²⁷ Buck Consultants. El Paso Firemen's Pension Fund: Actuarial Valuation. 1 January 2004. Buck Consultants. 12 June 2007. Dallas, TX.

²⁸ Feidner, Robert. Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

Note: A pension is a monthly payment from a fund division, such as the EPFPPF, to a retiree or beneficiary. This differs from a benefit in that “pension” specifically refers to retirement funds while the term “benefit” is usually more broadly defined. For purposes of simplicity, however, the terms will be used interchangeably in this report.

To qualify for normal retirement, an individual must have at least 20 years of credited service and must be at least 45 years old. Credited service years simply means the number of years the employee has worked for the department. If these conditions are met, the individual immediately begins receiving a pension upon retiring. The amount of pension a retiree receives is equal to 2.75% of the individual’s final wage, or the highest pay received by the individual in the last 12 months of employment before retirement. This is multiplied by their number of credited service years.²⁹ The minimum monthly pension a member of the fire department can receive is \$400; the minimum for a police officer is \$500.³⁰ Again the reason police officers receive a higher minimum pension, is because on average they contribute more to the fund.

The maximum amount of years an individual can contribute to the fund in regard to calculating their pension is 28 years. After this time, the individual’s contributions will not count toward determining the amount of pension they will receive upon retirement.³¹ The 28 year limit prevents a retiree from receiving a pension equal to more than 77% of his/her final wages. This figure is obtained by multiplying the 2.75% by the 28 years; it follows that:

$$\text{Maximum percent of Final Wages} = (28 \text{ service years}) \times (2.75\%) = 77\%$$

Take for example an employee who retires at 47 after 29 years of credited service and an ending monthly salary of \$4,500. His/her benefits would then be:

2.75% of his or her final wages, multiplied by his/her credited service years and months.³² This calculation is displayed in the following table:

Table X.X

Pension Calculation with More Than 28 Credited Service years

Accrual Rate	Final Wages	Credited Service Years	Total monthly pension
2.75% x	\$4,500 x	28 yrs =	\$3,465

Source: El Paso Fire and Police Pension Fund: Summary Plan Description

The following table shows the percent of final wages the pension equals. This percentage is found by dividing the monthly pension, calculated above, by the retiree’s final wages.

Table X.X

Percent of Final Wages

Monthly Pension	Final Wages	Percentage
\$3,465 /	\$4,500 =	.77 or 77%

Source: El Paso Fire and Police Pension Fund: Summary Plan Description

²⁹ City of El Paso. “El Paso Fire and Police Pension Fund: Summary Plan Description.” Directory of Pension Administration staff. El Paso: GPO, 2003.

³⁰ El Paso Firemen and Police Pension Fund. “Summary Plan Description: Fire.” 2007. El Paso Firemen and Police Pension Fund. July 2007. <<http://elpasofireandpolice.org/spdfire.pdf>>.

³¹ Feidner, Robert. Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

³² City of El Paso. “El Paso Fire and Police Pension Fund: Summary Plan Description.” Directory of Pension Administration staff. El Paso: GPO, 2003.

It is important to note again that even if an individual contributes to the fund for a total of 29 years or more, only 28 of these will be taken into account. However, according to Robert Feidner, Chairman of the El Paso Fire and Police Pension Fund, the vast majority of the police officers don't make it to their 25th year of employment³³ Calculating the retirement pension for anyone older than 45 years old is the same as above, since the monthly pension is based on their length of employment and individual salaries, rather than seniority.

Back DROP

The Back DROP, or deferred retirement option program, allows individuals who are at least 50 years old and have over 20 credited service years to exchange their normal retirement pension for a one time, lump sum payment and a reduced benefit. The lump sum the individual will receive is calculated by multiplying the individual's monthly pension by the months he or she wishes to participate under the Back DROP. The minimum amount of time an individual can choose to participate under the Back DROP is for a period of six months. The maximum time an individual can participate is 36 months. The reduced monthly pension is equal to the individual's pension at the beginning of the Back DROP period. In other words, the pension is calculated using the reduced credited service years. If the individual is less than 59 and one-half years old, the lump sum must be rolled, or transferred to a qualified Individual Retirement Account, or IRA. An individual must provide an advance written notice to the Pension Administration of the Pension Fund if he or she wishes to participate in the Back DROP. This pension could be beneficial to individual's who need more money after retiring.³⁴

Early Retirement

In order to qualify for early retirement, an individual must complete all requirements except the minimum age, or in other words obtain at least 20 years of credited service and be younger than 45 years old. Normal and early retirement pensions are essentially calculated the same way, except early retirement funds are subject to a withdrawal reduction. The reduction factor for early retirement is determined by the individual's age; the younger an individual is upon retirement, the more his or her pension will be reduced. Each age, in years and months, is assigned a decimal value. This value is multiplied by the pension they would have received from Normal Retirement. The resulting dollar amount is their Early Retirement pension.³⁵ The equation used to determine an individual's early retirement pension is almost the same as the equation used to calculate the normal retirement pension. The only difference in the two equations is the extra multiplication factor corresponding to an individual's age. For example: the pension for a 38 year old person with 28 years of credited service and a final monthly wage of \$4,500 will be calculated as follows (the retirement reduction factor for age 38 is 0.55)

Table X.X

Early Retirement Calculation

Percentage	Final Wages	Credited Service	Reduction	Total
2.75% x	\$4,500 x	28 x	0.55 =	\$1,905

Source: El Paso Fire and Police Pension Fund: Summary Plan Description

This pension is a little over half the amount of the example displayed in table X.X, where the individual had the same number of service years and salary, but was receiving normal retirement benefits. This is because the younger retiree will withdraw money for a longer period

³³ Feidner . Robert. Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

³⁴ El Paso Firemen and Police Pension Fund. "Summary Plan Description: Fire." 2007. [El Paso Firemen and Police Pension Fund](http://elpasofireandpolice.org/spdfire.pdf). July 2007. <<http://elpasofireandpolice.org/spdfire.pdf>>.

³⁵ El Paso Firemen and Policemen's Pension Fund. "Early Retirement Reduction Factors." 2007. [El Paso Fire and Police Pension Fund](http://elpasofireandpolice.org/errf.pdf). June 2007. <<http://elpasofireandpolice.org/errf.pdf>>.

of time, that the older individual, and so the benefit quantity must to be reduced in order for the pension fund to maintain balance.³⁶

As discussed above, early retirement requires at least 20 years of credit service. If for some reason an employee wishes to retire before this cut-off, there are some provisions set in place for them to receive a refund. A refund is a full reimbursement, without interest, of all the contributions an individual made to the fund during his or her membership.³⁷ For example, if an individual retires with a minimum of 5 credited service years, he or she can receive a refund on the contributions made to the pension plan. However, if an individual leaves before completing the required 5 years, they lose the right to a refund.

Disability Retirement

Disability retirement is available to individuals whom the EPFPPF Board of Trustees has determined to be permanently disabled, and are thus unable to continue work. The disability must have been acquired while in the line of duty, or must have been the result of an illness or injury for which the individual is not responsible. To validate the disability of the individual, medical proof must be provided from an independent medical examination. The pension the individual would receive under disability retirement is calculated the same as for normal retirement. The main difference is that there is no age requirement to qualify for disability retirement. In general the disability pension provided to the individual cannot be less than 50% of the individual's final wages. Some other limitations may also exist for certain individuals, to ensure that their pension complies with Internal Revenue Code (IRS) regulations.³⁸ In the event that an individual isn't permanently disabled and can still perform essential duties of their job, they may continue to work with workplace accommodations instead of accepting disability benefits.³⁹

Deferred Benefit

For individuals who do not have enough credited service years to qualify for the categories described above, but have at least ten years of credited service, a deferred benefit pension is available. This pension is provided through monthly payments and begins when an individual turns 50 years old. The contributions the individual has made to the pension plan cannot be withdrawn. If the contributions are withdrawn, as in early retirement, the individual will have forfeited eligibility for a deferred benefit pension. The amount of pension an individual will receive is determined by using the same equation for the normal retirement pension and under the same conditions. If an individual is 50 at the time he or she retires, the pension payments begin immediately. This benefit is essentially an opportunity for the individuals who didn't attain the required credited service years for the other benefit categories, to still receive compensation for their contributions.⁴⁰

Death Benefit

An individual becomes eligible to provide death benefits in regular payments to his or her spouse or children, if he or she dies as an active member or while eligible or receiving a pension. In order for a spouse to qualify for death benefits he or she must not have remarried and must have been married to his or her spouse prior to his or her retirement. If the spouse

³⁶ City of El Paso. "El Paso Fire and Police Pension Fund: Summary Plan Description." Directory of Pension Administration staff. El Paso: GPO, 2003.

³⁷ El Paso Firemen and Policemen's Pension Fund. "Summary Plan Description: Police." El Paso Firemen and Policemen's Pension Fund. July 2007. < <http://elpasofireandpolice.org/spdpol.pdf>>.

³⁸ El Paso Firemen and Policemen's Pension Fund. "Summary Plan Description: Police."

³⁹ El Paso Firemen and Policemen's Pension Fund. "Summary Plan Description: Police."

⁴⁰ Calderazzo, Michael. Vice-Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 12 June 2007.

had married the deceased individual after he or she had retired, they must have been married for at least two years to receive the death benefits.⁴¹

In order for the children of the deceased individual to qualify for the death benefits they must not be married and must be younger than 19 years old. If the child is a full-time student younger than 23, or is physically or mentally disabled, they also qualify for death benefits.

Death benefits are determined by the member's final wages before death, and cannot be less than 50% of those final wages. In the scenario where an individual dies while receiving normal, early, or disability retirement, the pension is divided amongst the spouse and/or children, with one-third going to the spouse and the remaining two-thirds being shared by the children. If the deceased individual had no children, or none of his children qualify, the spouse receives 100% of the pension the deceased individual was receiving. If the deceased individual has qualified children, but no qualified spouse, then the children equally divide two-thirds of the pension. As the children lose their qualifications, the pension amount has to be equally re-divided amongst the remaining qualified children.⁴²

In the event that an individual doesn't have a spouse and or children, he or she can designate through writing any beneficiary or estate who will receive the funds. This beneficiary would receive a lump-sum amount which will refund the contributions the deceased individual made to the pension fund.⁴³

Cost of Living Adjustment

Cost of living adjustment (COLA) is a service provided to retirees that increases their monthly pension every year in order to keep up with inflation and the rising price of goods and services. COLA begins for a fire department retiree once he or she reaches the age of 60. COLA begins for police department retirees at the age of 57.⁴⁴ COLA is compounded annually at a rate of 3%. In other words, once the COLA begins, an individual's pension will be increased annually at a rate of 3%. This is done every year in January. The table below illustrates how the COLA works over three years for an individual with a beginning monthly pension of \$2,000.⁴⁵

Table X.X

COLA increase by year

Year	Monthly Pension	COLA	Increase to monthly pension
2004	\$2,000.00	3%	\$60.00
2005	\$2,060.00	3%	\$61.80
2006	\$2,121.80		

Source: El Paso Fire and Police Pension Fund: Summary Plan Description

The automatic COLA is considered to be one of the major causes of the current underfunding as it often exceeds the increase in the average retiree's cost of living, thus paying more than necessary.⁴⁶

⁴¹ City of El Paso. "El Paso Fire and Police Pension Fund: Summary Plan Description." Directory of Pension Administration staff. El Paso: GPO, 2003.

⁴² City of El Paso. "El Paso Fire and Police Pension Fund: Summary Plan Description."

⁴³ El Paso Fire and Police Pension Fund: Summary Plan Description

⁴⁴ Calderazzo, Michael. Vice-Chairman: El Paso and Police Pension Fund. Personal Interview. 12 June 2007.

⁴⁵ City of El Paso. "El Paso Fire and Police Pension Fund: Summary Plan Description." Directory of Pension Administration staff. El Paso: GPO, 2003.

⁴⁶ Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

The benefits described above, including COLA, are regulated and maintained by a local board of trustees. The board of trustees is in charge of maintaining the fund in terms of financial upkeep and management. They must also make changes as they see fit and communicate with the city, their actuary, and the fire and police department members in order to keep the fund up-to-date. An *actuary* is an accountant responsible for reviewing and predicting the fund's financial performance using statistical records.

The Board of Trustees

The El Paso Fire and Police fund's Board of Trustees is comprised of 11 members. The board includes:

- The Mayor
- The fire and police chiefs or their designated representatives
- Two citizens appointed by the Mayor
- Three policemen
- Three firemen.⁴⁷

The two appointed citizens and the six fire and policemen serve a term of four years. Rules and regulations regarding the fund may be amended by majority vote from both the board of trustees and the fire and policemen as the board sees fit.⁴⁸ According to Executive Director of the fund and secretary of the board of trustees, Robert Stanton, the correct process to approve a change is from the board of trustees, to the fire and police members, then to the actuary and finally to city council.⁴⁹ The actuary for the EPFPPF is currently Richard Mackesey of Buck Consultants. When a change is put before an actuary, the actuary must view how the said change will impact the funding status and how many years until the change takes full-effect on the fund.⁵⁰

If city council rejects the request for change, the membership could then appeal for the citizens to vote on the issue. If the voters approve the change, then the plan will be amended. The board is also responsible for operating and keeping track of the balance of the pension fund, which includes hiring investment managers and numerous legal, actuarial, and consulting professionals.⁵¹

In order to further understand the structure and function of the EPFPPF as well as the negative outcomes that can result from an underfunding, Community Scholars looked into other pension plans that could provide better context to El Paso's underfunding situation.

Similar Pension Scenarios

To better understand the pension situations in El Paso, Community Scholars looked into other pension underfunding situations occurring outside of El Paso. Because of the similarity in mistakes made by administration and the revisions implemented, the underfunding situations

⁴⁷ City of El Paso. "Fire and Police Pension Fund Board of Trustees." The City of El Paso Website. 5 June 2007. <http://www.ci.el-paso.tx.us/muni_clerk/detail.asp?id=41>.

⁴⁸ El Paso Firemen and Policemen's Pension Fund. "City of El Paso Firemen and Policemen's Pension Fund." El Paso Firemen and Policemen's Pension Fund. 12 June 2007 <<http://www.elpasofireandpolice.org/PlanDoc.pdf> >.

⁴⁹ Stanton, Robert. Executive Director: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

⁵⁰ Mackesey, Richard. Actuarial Advisor: Buck Consultants. Phone Interview. 26 June 2007.

⁵¹ City of El Paso. "Fire and Police Pension Fund Board of Trustees." The City of El Paso Website. 5 June 2007. <http://www.ci.el-paso.tx.us/muni_clerk/detail.asp?id=41>.

occurring with the San Diego City Employees Retirement System and the Houston Municipal Employees Pension System were examined.

San Diego Pension Crisis

According to San Diego city attorney Michael Aguirre's 2005 interim report, the San Diego City Employees Retirement System (SDCERS) is suffering from a funding deficiency. This retirement fund currently has a \$1.37 billion deficit, a figure El Paso could face if nothing is done.

Structure of the San Diego City Employees Retirement System

The SDCERS is a defined benefit plan, like the EPFPPF and the EPCEPF. Monthly allowances are determined with the same basic formula as the El Paso plans. In San Diego actuaries perform regular analysis of the fund to make estimates concerning pay raises, incentive pay, and cost of living adjustments.⁵² Under this plan, it is also the responsibility of the actuary to decide the amount the city and employees need to contribute to the fund. This is determined by considering the total benefits that will be distributed that year and the finances needed to cover expenditures in assets and liabilities, also known as the Unfunded Actuarial Accrued Liability (UAAL). Based on this information the member and city contributions are determined.⁵³

If El Paso needs an example of how bad the situation can get and what not to do, San Diego provides a very good example. The SDCERS has been experiencing financial trouble for more than six years and has been exposed to many proposed solutions. Like the El Paso pension plans, San Diego leaders had to identify the factors that led to their underfunding problem and then propose courses of action to take to remedy the problem. This was completed in August 2004 and led to a settlement between the city of San Diego and the SDCERS. The actuarial evaluation stipulated that the city make full contributions to the fund starting in 2006, with up to \$500 million per year until 2008.⁵⁴

The pension crisis was so bad in San Diego that it led to investigations by the Securities and Exchange Commission and the U.S. Attorney's office. The scrutiny surrounding the situation eventually led San Diego Mayor Dick Murphy to resign from his position.⁵⁵ The investigations were also directed toward the pension's board of trustees, and in the end six trustees were charged with violating a conflict-of-interest law for voting for measures that benefited them financially.⁵⁶ In contrast, there has been no legal action taken concerning the under-funding problem with the EPFPPF and does not appear that there will be. El Paso will want to avoid San Diego's crises at all cost, because eventually the money will have to be paid, and if not taken care of sooner than later, will grow into critically large amounts that become the center of all political and social interests instead of other equally important issues.

Houston Pension Fund Under-funding

⁵² Calderazzo, Michael. Vice-Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 12 June 2007.

⁵³ Aguirre, Michael. "Interim Report #3." 9 April 2005. Violations of State and Local Laws Related to the SDCERS Pension Fund. 6 June 2007. <<http://www.sandiego.gov/cityattorney/reports/pdf/interimreport3.pdf>>.

⁵⁴ Maco, Paul S. and Richard C. Sauer. "Future of Contributions and Funding Status." The City of San Diego California's Disclosures of Obligation to Fund the San Diego City Employees' Retirement System and Related Disclosure Practices 1996-2004. 16 Sept. 2004: 29.

⁵⁵ Gelinias, Nicole. "A Permanent Pension-Fund Fix for San Diego." The San Diego Union-Tribune. 1 June 2005. 21 June 2007 <http://www.signonsandiego.com/uniontrib/20050601/news_lz1e1gelinias.html>.

⁵⁶ Briggs, Lisa. "Pension Charges Are Just the Beginning." The San Diego Union-Tribune. 22 May 2005. 25 June 2007 <http://www.signonsandiego.com/uniontrib/20050522/news_lz1e22pension.html>.

Houston provides a Texas example of another city undergoing a pension crisis. During a September 2004 meeting of the Texas Pension Review Board, Houston Mayor Bill White, revealed that there were \$2 billion in unfunded liabilities for the Houston Municipal Employees Pension System (HMEPS). Mr. White stated that the causes of the problem included a lack of independent audits by an actuary as well as a lack of financial expertise in the pension administration.⁵⁷ Unlike the EPFPPF, taxes could not be raised due to a city limitation, so the system's board came up with the following solutions.

Revisions

The following actions were taken after the 2004 Texas Pension Review Board meeting:

1. **The employee contribution was increased**
2. **The required retirement age was increased**
3. **Municipal employees and police officers received a salary raise-** the higher the employee salary is, the more money they contribute to the fund.
4. **By 2007, \$99 million in bonds would be sold-** Profits from these bonds will be a part of the contribution the city makes to the fund.
5. **A private sector task force was hired to propose changes to the management of the fund to ensure expertise in changes to policies made by city administration.**⁵⁸ The lack of experience in finance amongst administrators resulted in poor decisions concerning the investment and distribution of funds, so experts in this area were hired to fix the mistakes.

As of 2007, the above resolutions have helped Houston cut its underfunding in half. However, the city of Houston is still having trouble finding the funds to finance the remaining shortfall. The money to cover the remaining \$1 billion underfunding is instead being used to hire more police officers, pay for police academies and overtime as well as pay increases in the fire department.⁵⁹ City employees are also being given a 20% increase in health insurance within the next two years. San Diego mayor, Bill White, plans on proposing a second idea to the Board of Trustees that does not require employees to contribute a percentage of their salaries to the fund, terminating almost 400 jobs, or increasing the property taxes-- which are currently the other options. In the fiscal years 2005-2007, the city's contributions will be part the city budget and will also come from the sale of pension obligation bonds.⁶⁰ The obligation bonds are the same option El Paso is currently using, which will be discussed later.

El Paso Fire and Police Pension Fund History

A look at the history of the pension fund will help to better understand its current underfunding. The El Paso Fire and Police Pension Fund (EPFPPF) was established in the early 1930's in order to provide adequate retirement coverage to police and fire department retirees at the end of their service.

In the early years of its formation the fund began to experience some instability and in 1962 the city requested a study to be performed by the city actuary, to illuminate causes for the fund's financial instability. After its study, the actuary suggested that the city increase its contribution by levying a special tax which voters had already approved. This tax would help

⁵⁷ Stiles, Matt. "City Can't Keep Its Promise To Pension Fund." Houston Chronicle. 14 May 2007. 14 June 2007 < <http://www.chron.com>>.

⁵⁸ Rowe, Shad. "Report and Discussion on Houston Municipal Retirement System." 23 Sept. 2004. Texas Pension Review Board. 14 June 2007. <<http://www.prb.state.tx.us/tools/minutes/040923.pdf>>.

⁵⁹ Stiles, Matt. "City Can't Keep Its Promise to Pension Fund." Houston Chronicle. 14 May 2007. 14 June 2007 < <http://www.chron.com>>.

⁶⁰ Houston Municipal Employees Pension System. "Employer Contributions." Jan 2005. Houston Municipal Employees Pension System Benefits Handbook. 27 June 2007. <http://www.hmeps.org/publications/benefits_handbook_2005.pdf>.

alleviate some of the problems. From a period between, 1980 to the 90's the fund called for additional audits by its personal actuarial consulting company Watson Wyatt. During this time, Watson and Wyatt informed the board of trustees that based on their audits the plan was performing well and that the financial state was no longer problematic.⁶¹ This assurance by Watson Wyatt was later found to be inaccurate when the city conducted an independent actuarial audit in the mid-1990's.

According to ex-chairman of the EPFPPF board of trustees, Jake Soteriou, Wyatt's use of outdated mortality tables was one of the factors that created the current underfunding. A mortality table is set of statistics that is used to predict the life expectancy of the fund's members and thus the amount of money each will receive over the course of their retirement.⁶² Having an accurate mortality table allows planners to have a good idea of the amount of resources they will need in the future. It can be thought of in much the same way a traveler may plan out a long trip ahead of time taking into consideration the price of gas, food, hotels, etc. If the traveler uses inaccurate estimates for these commodities, he will soon find himself well into the trip before realizing that his money will run out before the trip is over. Similarly, using outdated mortality tables causes problems because it doesn't allow the pension planners to properly account for future expenses. If mortality is not accounted for properly, planners will not accurately predict the length of time retirees will need to be paid. This of course is something that needs to be considered and prepared for well in advance of the fact so that the money is available when the time comes. So for example, if a mortality table recorded the average death of employees as 70, and retirees don't actually die until age 75 on average, then the fund ends up paying out money longer to many people than originally predicted. The issues caused by the Wyatt actuary led the board to hire a new actuarial company, Buck Consultants, in 1996.

The City's independent study showed that because of outdated mortality, insufficient funding, and excessive spending, the pension fund would not be able to fulfill its financial obligations to future Fire and Police Department retirees. In fact in 1998, after monitoring the fund since 1992 the Texas Pension Review Board suggested that employee and city contributions to the fund be increased in order to begin to reverse the pension shortfall.⁶³ In the years that followed that assessment, the pension board of trustees spoke with many local leaders including past mayors and city council members to begin to fix the problem. However, no action was taken until recently due to other political priorities at the time. Now, because of insufficient action early on, the current pension fund is \$365 million underfunded and requires additional city and employee funding, as well as revisions to the plan.⁶⁴ One of the biggest lessons the City has learned from past mistakes is that time is of the essence. To explain, it is estimated that for every day the problem goes unsettled the deficiency will increase by roughly \$76 thousand.⁶⁵

Addressing the Problem: Proposed Action

To address the underfunding problem and figure out a way to alleviate it, the pension fund's board of trustees and the city came together to create a new plan in March 2002. The board hired two law firms that specialize in government retirement laws to assess the fund's

⁶¹ El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan." 5 March 2002. [El Paso Fire and Police Pension Fund](http://www.elpasofireandpolice.org/release.htm). June 2007. <<http://www.elpasofireandpolice.org/release.htm>>.

⁶² Soteriou, Jake. Ex-Chairman: El Paso Fire and Police Pension Fund. Phone Interview. 20 June 2007.

⁶³ El Paso Firemen and Policemen's Pension Fund. "Summary of the Funding Problem." [Texas Pension Review Board](http://www.prb.state.tx.us/news/epfp.html). 7 June 2007. <<http://www.prb.state.tx.us/news/epfp.html>>.

⁶⁴ El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan." 5 March 2002. [El Paso Fire and Police Pension Fund](http://www.elpasofireandpolice.org/release.htm). June 2007. <<http://www.elpasofireandpolice.org/release.htm>>.

⁶⁵ KVIA.com. "City Looks to Fix PD and FD Pension Fund. Tax Payers Could be Hit." 5 March 2007. [KVIA](http://www.kvia.com/global/story.asp?s=6076836&ClientType=Printable). 8 June 2007. <<http://www.kvia.com/global/story.asp?s=6076836&ClientType=Printable>>.

shortcomings and pinpoint the root of the problem. The law firms were the Robert D. Klausner Law Firm of Plantation, Florida, and the Lawton & Fields Law Firm of Dallas, Texas. After their assessment of the fund, both firms concluded that the city has been underfunding the pension for over 40 years by not levying a tax voters had previously approved. According to Chairman, Robert Feidner, the tax was never implemented due to a lack of political courage from city officials at the time, since taxes are unpopular.⁶⁶ The firms also concluded that without additional budget enhancement from the members and the city, they would not be able to undo the decades of underfunding.⁶⁷

At the advice of the Robert D. Klausner and the Lawton & Fields law firms, the Board of Trustees advocated the following actions take place in order to addresses the underfunding issue:

- Confer with the former actuary to discuss and improve the damages to the fund.
- Ask the City to add to its contribution to the fund
- Work with the fund's present actuary, Buck Consulting, to re-examine the proposed plan and guarantee accurate reporting of employee data from the city
- Alert the citizens of El Paso of potential danger to their well-being and safety in the community if this problem goes unfixed, as well as ask for their cooperation in addressing the situation at hand.
- As a final alternative, take proper legal action against the city if it fails to meet the newly set forth obligations to the fund.⁶⁸

The above actions helped lead to a new plan that consists of benefit cuts, contribution increases, the sale of pension obligation bonds, and a new second-tier plan for future members. The new second-tier plan also includes a change to the automatic COLA and accrual rates. The following section will discuss this new plan.

El Paso Fire and Police Pension Plan Revisions

Repairing the Fund and the New Plan

In order to repair and secure the EPFPPF's \$365 million shortcoming, a new pension plan was devised by the city and the board of trustees in the spring of 2007. One of the actions proposed by the plan that will be implemented is that the underfunded amount be split between the board and the city. The new plan also cuts retiree benefits while increasing contributions. In addition, the new plan makes changes to contribution refunds, disability pension, and COLA. All of these measures were considered necessary to prevent the underfunding from reaching a predicted \$650 million over the next ten years and \$1.4 billion by 2027.⁶⁹

The main course of action to cover the bulk of the underfunding will be the city's sale of pension obligation bonds. Obligation bonds are loans from financial institutions that are to be repaid within 30 years, including interest. Currently, the city has arranged a \$210 million contribution through two pension obligation bond sales. The first sale occurred in July 2007 for \$100 million, and the second will occur in July 2009 for \$110 million.⁷⁰

⁶⁶ Feidner, Robert. Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

⁶⁷ El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan." 5 March 2002. [El Paso Fire and Police Pension Fund](http://www.elpasofireandpolice.org/release.htm). June 2007. <<http://www.elpasofireandpolice.org/release.htm>>.

⁶⁸ El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan."

⁶⁹ El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan."

⁷⁰ Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

Details of the Revision

According to the new plan, any new person hired as a fireman or policeman automatically falls under the new pension plan and will routinely contribute to it through payroll deductions. This money goes toward the pension they will receive upon retirement. Normal retirement requirements have been changed from a minimum age of 45 years old and 20 minimum credit service years to a minimum age of at least 50 years of age with 25 years of service.⁷¹ The member contribution rates were also increased by 2%, meaning that firemen are now required to contribute 15.28% of their paychecks, while policemen contribute 13.89%.⁷²

As with the former plan, the new plan still covers disability benefits. Eligibility for this type of retirement is determined the same as it was before the revisions. The disability pension granted to those injured in the line of duty is tax deductible. Another major change is that in calculating benefits, the retiree's "final wages" are no longer defined as the highest salary they received in the last 12 months, but rather as the average of their salary from the last 36 months of employment.⁷³ This change was made to prevent eligible employees from retiring immediately after receiving a raise to take advantage of the increased benefits. Now they no longer have that incentive unless they are truly ready to retire.⁷⁴

As mentioned previously one of the major problems with the pension fund is the Cost of Living Adjustment (COLA), which factors in an annual 3% increase to a retiree's monthly pension to adjust for inflation and the rising price of goods. Initially, the city sought to cut out COLA entirely, but the pension board firmly refused.⁷⁵ According to Deputy City Manager, Bill Studer, the automatic COLA was one of the major causes to the underfunding issue because it surpasses the rate of inflation and ends up paying out more money than needed. According to him, the purpose of the COLA is to allow retirees to keep up with a shifting market, not to surpass it.⁷⁶ A summary of the plan changes as discussed above is presented as follows:

- Increase required credited service years from 20 to 25 years
- Increase retirement age from 45 to 50
- "Final wages" is defined as the average of the last 36 consecutive months of employment
- Increase the rate of contribution for the police workforce to roughly 14%
- Raise the contribution rate for the fire workforce to roughly 15%.⁷⁷

The next section will discuss *second tier* benefits which are a new component added to the revised pension fund plan for new members.

Second-Tier Benefits

The new plan will also contain a "second tier" benefits plan for future members. Some benefits within the second-tier plan will be the equal to those in the current employee's pension, while some changes will only apply to future members. As stated in the new plan for current employees, future firemen and policemen will become automatic members to the pension fund.

⁷¹ El Paso Firemen and Policemen's Pension Fund. "City of El Paso Firemen and Policemen's Pension Fund." [El Paso Firemen and Policemen's Pension Fund](http://www.elpasofireandpolice.org/PlanDoc.pdf) . 12 June 2007. <<http://www.elpasofireandpolice.org/PlanDoc.pdf> >.

⁷² El Paso Firemen and Policemen's Pension Fund.

⁷³ El Paso Firemen and Policemen's Pension Fund.

⁷⁴ Calderazzo, Michael. Vice-Chair: El Paso Fire and Police Pension Fund. Personal Interview. 12 June 2007.

⁷⁵ Calderazzo, Michael.

⁷⁶ Studer, William. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

⁷⁷ El Paso Firemen and Policemen's Pension Fund. "City of El Paso Firemen and Policemen's Pension Fund." [El Paso Firemen and Policemen's Pension Fund](http://www.elpasofireandpolice.org/PlanDoc.pdf) . 12 June 2007. <<http://www.elpasofireandpolice.org/PlanDoc.pdf> >.

Their contributions will be deducted automatically from their payroll at the same percentage as current employees. Contribution refunds, like the current members' refunds, will only be granted to those who have completed at least five years of service.⁷⁸ The second-tier changes for future members are as follows:

- Decrease in survivor benefits from 100% to 75%
- Reduce the future accrual rate to from 2.75% to 2.5%
- Increase retirement eligibility to age from 45 to 50 with 25 years of credit service
- COLA will no longer be automatic post-retirement.⁷⁹

By reducing the future member's accrual rate, which is the percentage used to determine the pension amount, from 2.75% to 2.5%, the maximum amount of benefits to be received upon retirement will be reduced from 77% to 70%, as shown below.

Table X.X

Accrual Rate of the Old and Revised plans

	Accrual Rate	Number of Credit Service Years	Percent of Final Wages
Old Plan	2.75%	X 28	77%
New Plan	2.50%	X 28	70%

Source: El Paso Firemen and Policemen's Pension Fund

Again, final wages are calculated by multiplying the accrual rate percentage by the number of service years.

Effects of the EPFPPF Revision

With new revisions and a second-tier plan, there are expected to be some effects that are less desirable than others. For example, property tax must be increased. Homeowners may be relieved to know that the increase is only expected to be about one or two cents.⁸⁰

According to the El Paso Fire and Police Trustees Action Plan, public safety is also directly endangered by this underfunding issue. If the fire and police workforce is affected significantly by the underfunding for example, it could easily effect the public's overall safety, because less recruits may be attracted to a seemingly unstable system.⁸¹ According to William Studer and several others, the real problem won't necessarily be recruitment, but rather retention. He suggests that that young people are thinking more about having a job and earning money than they are about retirement. On the other hand, more established and older employees have more concern for their impending retirement, and thus the bigger problem is retaining current employees and keeping them from transferring or retiring early.⁸²

For a growing city this could be a problem, because as the population grows the need for these public safety services also increases.⁸³ For example, with the Base Realignment and

⁷⁸ El Paso Firemen and Policemen's Pension Fund. "Fire Division." 1 July 2007. City of El Paso Firemen and Policemen's Pension Fund. 12 June 2007. <<http://www.elpasofireandpolice.org/PlanDoc.pdf>>.

⁷⁹ El Paso Firemen and Policemen's Pension Fund. "City of El Paso Firemen and Policemen's Pension Fund." El Paso Firemen and Policemen's Pension Fund. 12 June 2007.<<http://www.elpasofireandpolice.org/PlanDoc.pdf>>.

⁸⁰ Novick, Daniel. "Pension Plan Problems Solved." 13 Feb 2007. KFOX-TV. 8 June 2007. <<http://www.kfoxtv.com/news/11004864/detail.html?taf=elp>>.

⁸¹ Feidner Robert. Chairman: El Paso Fire and Police Pension Fund. Personal Interview. 19 June 2007.

⁸² William Studer. Deputy City Manager: City of El Paso. Personal Interview. 19 June 2007.

⁸³ El Paso Firemen and Policemen's Pension Fund. "El Paso Fire and Police Pension Trustees Adopt Action Plan." 5 March 2002. El Paso Fire and Police Pension Fund. June 2007. <<http://www.elpasofireandpolice.org/release.htm>>.

Closure (BRAC) Act of 2005, there is expected to be over 60,000 troops and family members living in the El Paso area. Along with these people, new high-tech jobs are expected to follow, giving our region an estimated economic boost of \$4 billion annually.⁸⁴ This growth can be threatened if not enough police and fire personnel are present to provide safety for these new residents and businesses.

After looking into the EPFPPF's history and underfunding situation, as well as the new changes for current and future members, Community Scholars decided to also look into the El Paso City Employees Pension Fund and their underfunded predicament.

Structure of the El Paso City Employees Pension Fund

Similar to the EPFPPF, the El Paso City Employees Pension Fund (EPCEPF) is also a defined benefit plan, and is currently underfunded \$103 million. This is almost less than one-third of the EPFPPF's total underfunding but significant nonetheless.⁸⁵ An actuarial evaluation performed by the same actuary as the EPFPPF, Buck Consultants, revealed that reasons for the underfunding included inadequate employee contribution rates and a longer life expectancy for members than predicted by mortality tables—basically the same issues the EPFPPF experienced. Again, retirees are living longer and so more benefits are being allocated for a longer period of time. Another factor that contributed to the underfunding was the stock market falling slump between 2000 and 2001 that also affected the EPFPPF along with other pension throughout the nation.

A depreciated stock market causes an insufficient investment return of a pension fund's assets, which negatively affects the financial status of the fund. This means that less money is being placed into the fund through expected investment returns than is needed to keep up with the benefits paid.

Benefits

As with the EPFPPF, members of the City's pension fund are also entitled to certain benefits. Unlike the members of the EPFPPF, however, the members of the EPCEPF are civilians and thus are also eligible for Social Security. This means that retired members of El Paso City's pension fund receive two checks per month.⁸⁶ The EPCEPF also distributes disability benefits through requirements that are similar to the EPFPPF. The criteria for earning retirement benefits includes being 55 years of age and 10 years of credited service. These benefits are calculated using a similar formula to that of the EPFPPF, which is the product of 2.5% times the number of credit service years and the highest salary the individual received during their employment.

Solutions to the Insufficient Funding

Currently, the EPCEPF is 84% funded, and with only a \$103 underfunding, the Board of Trustees hopes to achieve 100% funded status by 2012. As this underfunding is not as drastic as that of the EPFPPF, fewer actions are necessary to recover. Basically, City Council has decided to simply raise the city's contribution to the fund by 1.4 % and employees' contribution by 1%. This means the city now contributes 11.65 %, while employees contribute 7.75% of their payroll into the fund.⁸⁷ With this set-up in place the City's underfunding should be back in good

⁸⁴ Reyes, Silvestre. "High-Tech Jobs Coming to El Paso." 2006. U.S. Representative: Silvestre Reyes. 2007. <http://www.house.gov/reyes/news_detail.asp?id=915>

⁸⁵ Sandoval, Juan F. Chairman: El Paso City Employees Pension Fund. Personal Interview. 21 June 2007

⁸⁶ Sandoval, Juan F.

⁸⁷ Sandoval, Juan F.

health by 2012. In terms of the two funds, the City has managed to fare better than the EPFPPF simply due to better management through the years. For both funds, it will be important to maintain a strong management of the fund to ensure its future success.

Summary

The City of El Paso has experienced a pension crisis for its fire and policemen as well as its city employees. These problems stemmed from poor leadership and oversight in years past, but are now being addressed. With the current plans for this issue set in place, the problems with both pensions should be resolved in the allotted timeframes. However, it will be important for future local governments and pension leaders to learn from past mistakes to ensure that these same issues do not arise again or escalate to the magnitude of the pension underfunding in San Diego or Houston.

With the general trend of baby boomers out-populating the younger generations, pensions across the nation including social security are searching for solutions to remedy the problem. It will be of utmost importance for current planners to take all of these factors into consideration in their management of the pension funds so that the vital services provided by city workers and especially the policemen and firemen do not suffer.

Conclusions

- 1. The underfunding problem in the El Paso Firemen and Policemen's Pension Fund arose in the 1960's, though it wasn't addressed until recently.** In years past, the underfunding was less than it is today. The problem would have been easier to resolve at that time with improved communication and further political courage.
- 2. If the underfunding continues to increase, it will eventually reach \$650 million in 10 years.** Chief of Police, Richard Wiles was quoted in a KVIA interview as saying that the underfunding grows at a rate of \$76,000 every day. This shows the importance of addressing the problem before the total exceeds half a billion dollars and nearly twice the city's annual budget.
- 3. The funding period to resolve the \$365 million fire and police pension underfunding problem is 40 years.** An actuarial evaluation of the fund completed by Buck Consultants revealed that it will take 40 years with revisions to resolve the problem and obtain a 90% funded status.
- 4. Because the plan is defined-benefit, a retiree's pension doesn't rely on the performance of investments in the stock market.** A member's retirement pension is based on the number of credited service years attained and his or her final wages. The investments the Pension Fund makes in the stock market, and the interest earned from these investments do not directly affect the members' retirement pension.
- 5. Police officers contribute less to the fund than firemen.** From our research, we have discovered that firemen are required to contribute 2% more of their salaries to the fund than policemen. The reason for this difference in contribution rates is that there are a higher number of policemen in the workforce than firemen.
- 6. The increase in property tax as a result of the City's contribution to the fire and police pension fund will be minimal.** Deputy City Manager, William Studer, stated that the city's property tax will be increased by a minimal amount of 2%. According to him, this will only be a small effect on taxpayers.

- 7. The El Paso City Employees Pension Fund is expected to be fully funded in five years.** During a personal interview with Juan F. Sandoval, Chairman for the El Paso City Employees Pension Fund, he stated that by increasing member contribution rates the fund will achieve 100% funded status in five years.

Recommendations

Based on the research and the conclusions, Community Scholars recommends the following actions be taken in regard to the EPFPP.

- 1. All Board of Trustees members should be well informed in the areas of finance and investment.** According to Houston City Mayor, Bill White, being unaware of proper investment strategies leads to poor returns and an increase in underfunding. In order to prevent this from happening to the El Paso Fire and Police Pension Fund, Board of Trustees members need to become more aware of proper investments and accurate financing.
- 2. The Fire and Police departments should increase information and incentive to care to employees concerning the El Paso Fire and Police Pension Fund.** All employees and members of the fund need to be completely informed on the fund's status, as well as care about the complications the fund may be experiencing at any given time.
- 3. In the event of another under-funding issue in the future, authorities should address the problem immediately in order to prevent increased complications.** According to Deputy City Manager, William Studer, if the financial problems had been addressed in the past, there would not be a \$365 million underfunded amount now forcing the EPFPPF to increase contributions and cut benefits. Instead of pushing the problems back year after year, there needs to be resolutions immediately.
- 4. When developing a method to fix an underfunding situation, always consider what can be done in case the problem is not solved or other problems arise.** According to vice-chair of the EPFPPF, Michael Calderazzo, if this new plan fails, there is no alternate plan. Community Scholars believes that there should be multiple plans as backup in the case of unforeseen incidents.
- 5. Information that appears on the web site should be routinely updated and accurate so as to provide both department members and the general public with sufficient and adequate information.** The El Paso Fire and Police Pension Fund website should not have a disclaimer that makes no warranties for the accuracy, timeliness, completeness, usefulness, or adequacy of the information provided.
- 6. The City of El Paso and the El Paso Firemen and Policemen's Pension Fund should maintain proper communication with each other and the community in order to prevent the issues of the past and present occurring again in the future.** Communication is the key to have a well-rounded system to insure that problems will not re-occur due to negligence or miscommunication from either party. Cooperation can assist in minimizing problems that may occur or develop into a crisis.

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