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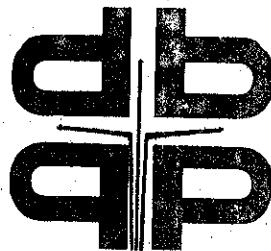
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*File Pension  
Funds*

Jack Bigel  
president

Proposal Submitted to

The Department of Housing and Urban Development  
in Response to

Request for Grant Applications H-2921 - RG

**AN ECONOMIC ANALYSIS OF STATE AND LOCAL PENSION ISSUES:**

**THE IMPACT OF ALTERNATIVE POLICY DECISIONS**

Organization : Program Planners, Inc.  
230 West 41st Street  
New York, N.Y. 10036

Amount Requested : \$322,374

Proposed Duration : 24 months

Project Director : Jack Bigel

Principal Investigator : Anthony Gajda

Classification of Organization : Profit-making

August 30, 1978

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ABSTRACT

Program Planners, Inc. proposes to conduct an economic analysis of state and local government pension funds. The research methodology incorporates an economic model of pensions, a general actuarial model, and empirical investigation. The research will be accomplished in four stages: Level of Funding; Asset Management; Compensation Levels; and the Future of State and Local Government Pensions, and will be completed over a two-year period.

The following summarizes the objectives of each of the four stages of research.

- I. The Level of Pension Funding: The specification of a general economic model and a general actuarial model and the investigation of expected fiscal and efficiency implications of changes in various components of the pension agreement will constitute the first stage of the study.
- II. Asset Management: Historic and comparative analyses, along with reasonable projections of a program to develop incentives for socially desirable investments, will be evaluated in terms of expected future investment results. Portfolio analysis will be employed to estimate the results of various future investment programs. The conclusions regarding past, present and future asset management practices and policies will constitute the second stage of research.
- III. Compensation Levels: This stage will be comprised of a survey of current levels of public and private sector pension benefits and total compensation, the illustration of post-retirement income patterns, and the formulation of criteria for estimating the retirement income required to sustain a constant standard of living.

IV. The Future of State and Local Government Pensions: This stage will consist of the identification of the interdependencies and interrelationships of pension funding, asset management and compensation levels. Estimates of the effects of various policy modifications will also be presented.

Upon completion of the four stages of research, a final report will be prepared. This report will constitute a single source of essential financial and benefit policy data on public employee pension plans and identify the fiscal implications which must be considered before various policy modifications are incorporated into state and local government pension plans.

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BACKGROUND

The cost of public employee pensions to state and local governments is an issue of growing concern.

Unfortunately, analysis of public employee pension benefits and costs have usually been descriptive in nature and associated with static analysis and have not provided the analytical framework required for decision-making. The major papers on public employee pensions have dealt with the mechanics of pension fund operations (Bleakney[2]; Jump[5]; Thomas[7]) or with estimates of the liabilities and levels of funding (Bahl & Jump[1]). A recent paper on the optimum pension size and level of funding state and local government pensions (Mumy[6]) incorporates a discrete two-period model in order to develop a generalized theory of pensions. An exception is the analysis of the New York City retirement systems conducted by the Mayor's Management Advisory Board[4], commonly referred to as the Shinn Commission. The Shinn Commission, composed of pension professionals from the public, private, and labor sectors, examined the funding status, benefit and cost levels and histories of the New York City pension plans and performed comparisons with selected public and private sector pension plans.

However, the accumulation and analysis of data concerning public employee pensions generally is still in a primitive stage and is inadequate for the development of a public policy toward pension benefits.

The most probable reason for the dearth of information on state and local government employee pensions is the interdisciplinary nature of public employee pensions. A complete analysis of public employee pensions must include wage theory, public finance, portfolio analysis, actuarial theory, etc.

The diversity of interests in public employee pensions can best be demonstrated by the current issues affecting and affected by public employee pensions. Major issues in public employee pensions include the following:

1) Growth of Assets and Coverage. The rate of growth of public employee pension plans has approximated the rate of growth of private sector pension plans and has vastly exceeded early projections of the growth of public employee pension plans. Between 1966-67 and 1975-76, the assets and membership of public employee pension plans have grown by 184% and 28.6% while private sector pension plans have recorded a 171% growth in assets and a 40% growth in membership.\*

	<u>State &amp; Local Gov'ts.</u>		<u>Private Sector<sup>a</sup></u>	
	<u>Assets</u>	<u>Membership</u>	<u>Assets</u>	<u>Membership<sup>b</sup></u>
1966-67	\$ 39,265	7,068,213	\$ 59,180	19,100 <sup>d</sup>
1975-76	111,501	9,089,000 <sup>c</sup>	160,415	26,800
Change	72,236	2,020,787	101,235	7,700
% Change	184.0%	28.6%	171.1%	40.3%

Note: a. noninsured  
b. not including beneficiaries  
c. 1972 data  
d. 1965 data

In an early analysis of public employee pensions, P. Cagan[3] projected asset and membership levels, assuming continued growth in benefits and a 4.7% annual growth in employment levels. Even with his relatively liberal assumptions, Cagan's projections fell significantly short of the actual results.

\*Source: U.S. Bureau of the Census, Finances of Employee - Retirement Systems of State and Local Governments, 1966/67 Series 6F67, No. 2; 1975/76 Series 6F76 No. 2.

U.S. Bureau of the Census, Census of Governments, Employee Retirement Systems of State and Local Governments, 1967 and 1972.

U.S. Social Security Administration, Social Security Bulletin, November 1977.

State & Local Government Pension Plans

<u>Cagan</u>		<u>Actual</u>	
<u>Assets</u>	<u>Membership</u>	<u>Assets</u>	<u>Membership</u>
1965-66 \$34.1 B.	6.3 M.	\$ 35.2 B.	7.1 M. <sup>a</sup>
1975-76 \$81.0 B.	10.1 M.	\$111.5 B.	9.1 M. <sup>b</sup>

Note: a. 1967 data  
b. 1972 data

2) Pension and Expenditure Growth. The growth of pension costs, in absolute and relative terms, in state and local government budgets has drawn the increasing attention of fiscal officers and planners.

State & Local Governments \*

	<u>Pension Costs</u>	<u>Total Expenditures</u>	<u>Per Cent of Pensions to Tot. Expend.</u>
1965-66	\$ 2,630 M.	\$ 94,906 M.	2.77%
1975-76	10,502 M.	304,088 M.	3.45%
Change	7,872 M.	209,182 M.	.68%
% Change	299%	220%	24.55%

The growth in pension costs has led to the appointment of high-level pension commissions which have the mission of recommending changes in pension plans which will bring uniformity of administration and fiscal realism to pension plans. Those commissions now operate in at least ten states, including Massachusetts, New York, Wisconsin, Ohio, Minnesota, and Louisiana.

3) Regulation. On September 2, 1974, Public Law 93-406 (commonly referred to as E.R.I.S.A.) established

\*Source: US Bureau of the Census, Government Finances, 6F Series 7G # 5.

US Bureau of the Census of Governments, 1972 Vol.6, #4, Historical Statistics on Governmental Finances and Employment.

standards for the administration and performance of private sector pension funds. The major goal of E.R.I.S.A. is to ensure that the promise of pension benefits to employees is kept. Additionally, E.R.I.S.A. establishes minimum standards for eligibility, disclosure and reporting, and vesting. The extension of E.R.I.S.A., or E.R.I.S.A.-like, standards to state and local government pension plans was deferred, pending a survey and analysis of existing state and local government pension plan practices with respect to eligibility, vesting, funding, disclosure, etc.

That survey and analysis, conducted by the Pension Task Force of the House Subcommittee on Labor Standards, is now complete and will soon be issued.

While the Pension Task Force survey addresses the question of funding adequacy, it establishes no criteria or bench marks for determining whether a plan is adequately funded even though such standards are necessary for state and local government financial planning.

4) Role Of The Federal Government. The Federal government, through its Federal revenue-sharing and assistance programs, channels \$47,054 million<sup>a</sup> into state and local governments: an amount equal to 17.9%<sup>b</sup> of all state and local government receipts. Since state and local governments are free to use general revenue-sharing funds and some portion of other Federal monies in any way that they believe is necessary, a portion of those funds, either directly or indirectly, is used to finance employee pension benefits and, in that context, the Federal government is a partner in state and local government pension financing. Inasmuch as many state and local government pension funds are not fully funded, any reduction in Federal assistance may have important consequences on the stability of those pension funds.

Note: a. Statistical Abstract of the United States, 1977.

b. Ibid.

5) Government And Pension Plans. Pension funds, although autonomous in varying degrees, are associated with their sponsoring government entity. The soundness of the various state and local government pension plans, therefore, reflect on the soundness of the sponsoring governments, and vice versa. The most widely publicized example of the interdependence of pension plans and government is the New York City experience during the years 1974-1978.

The New York City fiscal crisis commentators footnoted their reports with statements on the relatively large underfunding of pension benefits because of the use of outdated mortality tables. It was only after an exhaustive analysis of the New York City pension funds by the Shinn Commission that the true actuarial condition of the pension funds was revealed: the relatively conservative assumptions with respect to mortality were nearly offset by the relatively conservative interest assumptions. Updating all of the outdated actuarial assumptions resulted in an increase in pension costs of less than 15%.

A second measure of the soundness of the New York City pension funds was their ability to invest \$2,500 million in New York City bonds with imperceptible disruptions in their portfolios. In contrast, if the New York City pension plans had not been soundly financed, the ability of New York City to avoid default and bankruptcy in 1975 would have been mortally limited.

Less publicized instances of government and pension plan interdependence exist, for example, in Texas municipalities where actual pension contributions are 1/3 of the actuarially - required contributions and where actuarial deficits have reached \$500 million<sup>a</sup>.

Only a comprehensive examination of state and local government pension plans will reveal the implications of the relationship between pension funds and sponsoring governments.

a. Annual Financial Report, City of Houston, Texas, December 31, 1977.

6) Income Constraints. The passage of Proposition 13 in California, the consideration of similar legislation in other states and municipalities, the fiscal crisis of N.Y.C. and the fiscal problems in other cities confirm that the already limited resources of state and local governments may be even further constrained.

The two-step process that has led to a 60% reduction of pensions of N.Y.C. and N.Y.S. employees<sup>a</sup> and the consideration of the reduction of pension benefits for many public employees in California<sup>b</sup> were and are expected to provide immediate fiscal relief. However, the judicial interpretation of pensions as contracts limits the relief that will inure to state and local governments by the reduction in pension benefits for future employees. In other words, even if pension benefits are reduced for future employees, several decades will pass before the full savings of benefit reductions are experienced.

7) Portfolio Management. One of the most powerful assumptions in the calculation of the cost of pensions is the expected rate of return on investments: the interest assumption. All other things being equal, if a portfolio manager can obtain a higher rate of return on pension fund assets then the cost of pension benefits will decrease. An often-proven rule-of-thumb, regarding the interest assumption, is that an increase of 0.5% in the interest assumption results in a 10-12% decrease in pension costs. Applying this rule-of-thumb to the pension contributions made by state and local governments in fiscal year 1976 (\$10,502 million) a .5% increase in interest returns would result in a savings in excess of \$1,000 million. Similarly, if, through improved portfolio management, the interest assumption can be increased by 0.5%, and if state and local government pension contributions are held constant, the actuarial condition of the pension plans will be enhanced.

Note: a. N.Y.C. Municipal Labor Committee Presentation to Senator William Proxmire, Dec. 28, 1977.

b. Los Angeles Times, July 3, 1978.

Improved portfolio management will, however, require a basic re-evaluation of investment philosophy. The general movement over the past several decades from relatively secure investments, e.g. U.S. Government securities, high-grade corporate and utility bonds, etc. toward securities with potentially higher rates of returns, e.g. equity investments, must be carefully reviewed. The relative performance of different types of investments, as well as the quality of investment advisors or counsel, must be quantified.

8) The Retiree Population. Because of health and technological advances, mortality rates have reduced. As a result of reductions in mortality, the elderly, non-working population is growing both absolutely and relatively.\*

	<u>Over - 65 Retired Persons</u>	<u>Retired State &amp; Local Government Employees</u>	<u>Total Population</u>	<u>% over 65 to Total Pop.</u>
1960	16,560,000	739,077 <sup>a</sup>	179,323,000	9.3%
1976	22,934,000	1,463,399 <sup>b</sup>	214,659,000	10.7%
Change	6,424,000	724,322	35,536,000	
% Change	38.5%	98.0%	19.7%	

Note: a. 1962 data  
b. 1972 data

To the extent that state and local government employees earn pensions during their working careers, those employees do not represent a resource drain or require assistance in their retirements.

The explicit promise of the pension agreement to pay a benefit in the future must be buttressed by adequate funding in order to deliver the security expected by retiring public employees.

\*Source: US Bureau of the Census, Census of Population 1960 Current Population Reports, Series P-25.

US Bureau of the Census, Census of Governments, 1962, & 1972, Employee Retirement Systems of State & Local Governments.

PURPOSE AND OBJECTIVE OF THE PROPOSAL

Because of the potential for exogenous restraints on the income of state and local governments, either by Proposition 13 and similar movements, or because of the apparent economic decline of areas and regions, or other factors, there must be a clear understanding of each of the elements of government expenditure. In that vein, most expenditures are straightforward: dollars are expended in the form of wages, or supplies, or heat and electricity, or transfer payments, etc. In addition, funds are borrowed in credit markets and debt service costs are articulated and disclosed. Less understood than any other form of government expenditure, though, is pension costs.

Although many disciplines have been concerned with the subject of public employee pensions, that concern has been directed at particular aspects of public employee pensions. The extant literature is generally descriptive in nature and deals with the following single issues:

- 1) benefit levels, both relative and absolute;
- 2) budget implications, although, little is known of the ultimate costs of pension benefits; and,
- 3) the need for uniformity in reporting the costs of pensions, etc.

The state of the art is such that there is no complete organization of the relationships between retirement income needs of employees, the cost concerns of both employers and employees, the implications of various funding arrangements, the implications of past funding deficiencies, etc. and, as a result, decisions may be made regarding pension benefits without a complete understanding of short-term or long-term consequences.

The purpose of this research project is to develop a complete economic model of state and local government pensions. That model will include:

- 1) an analysis of the trade-off between wages and pensions,
- 2) the impact on the employee of benefit levels,
- 3) an analysis of the legal status of pension benefits,
- 4) the merits of different approaches to paying for (funding) pension benefits, for both government and the employee,
- 5) the effects of pensions on wealth transfers and income distributions, and,
- 6) the relative efficiency of various asset management techniques in reducing the cost of pensions.

The objective of the research project is the development of a complete analysis of the public policy issues regarding state and local government pensions with a discussion of the alternative policies available to state and local jurisdictions.

Specific objectives of this proposal will be:

- 1) to identify the levels of compensation of state and local government employees along with the levels of compensation for comparable or equivalent private sector employees, with explicit identification of the value of pension benefits. Such data will give insight into the level of competition and competitive advantages of public and private sectors.
- 2) to design criteria for measuring the actuarial condition of state and local government pension funds and to present alternative methods, where necessary, for improvement of actuarial conditions. Generally, the funding standards required by E.R.I.S.A. for private sector pension plans may be more stringent than those necessary for employers whose institutional nature implies a continuous existence.
- 3) to organize and evaluate the results of various investment techniques and philosophies in order to identify the most efficient form of asset management. Such an evaluation will address the issues of security, risk, rate of return, social welfare, distribution effects and capital market implications in order to present optional programs of asset management.

4) to identify the implications of pension costs to state and local governments and their employees under various assumptions of change, i.e. growth or decline in employment levels, benefit levels, funding levels, and scope of government services.

The study will, for the first time, trace the evolution of pensions, from the initial estimation of retirement income needs, through the legislation of agreements, through the financing of costs, through the payment of pensions, with the impact on economic activity identified at each step of the process.

The intent of this research is to articulate and organize actuarial, public finance, and investment concepts in order to enhance the ability of pension plan sponsors to evaluate the fiscal, social and labor-management objectives and ramifications associated with public employee pension policy.

An understanding of the basis for pension demands and the implications of the pension agreement will permit public officials to prepare their financial plans with a greater awareness of costs.

A knowledge of the relative funding level of pension funds will assure employees of their ability to collect pension benefits or will stimulate concern for an improvement in the funding level.

The interested or concerned public will be served by the availability of information on the dynamics of state and local government pension benefits.

Clearly, the project will be an important contribution to a better understanding of an issue of growing concern to the sponsors, administrators and managers, and members and beneficiaries of the more than 6,000 state and local pension funds in the nation.

SUMMARY OF APPROACH

An economic analysis of fifty state and forty-six municipal government pension funds will be conducted. The research methodology will consist of an economic model of pensions, a general actuarial model and empirical investigation.

The economic model will serve as the framework for an empirical investigation of the effect of alternative policy decisions on state and local government pension plans. The research will be accomplished in four stages: Level of Funding; Asset Management; Compensation Levels and the Future of State and Local Government Pensions.

The first three stages of research will consist of pertinent data collection and analyses. Capital-labor ratios, hypothetical rates of return, hypothetical fund valuations and various criteria will be developed and utilized as research tools or for illustrative purposes during each stage of research. Comprehensive reports consisting of methodology, analyses, and findings will be prepared at the completion of each stage of research.

RESEARCH DESIGN AND STATEMENT OF WORK\*

The issues to be addressed in the study appear to be wide-ranging and, in some instances, there do not appear to be direct relationships, e.g. the impact, if any, of investments in "socially desirable assets," and comparative compensation; or, definitions of funding levels and pension benefit adequacy. Yet, there is a common thread: the agreement to pay a pension benefit at some time in the future.

The research methodology will incorporate an economic model of pensions, a general actuarial model, and empirical investigation.

The economic model will serve as the framework for an empirical investigation of various issues concerning or flowing from state and local government pensions, which will be accomplished in four stages:

- 1) the issue of pension funding,
- 2) the issue of asset management,
- 3) the issue of compensation levels, and,
- 4) the relationships between funding, compensation levels and asset management.

The fourth stage will consist of the identification of the interdependencies and interrelationships of pension funding, asset management and compensation levels.

Reports will be prepared at the completion of each of the four stages.

Economic Model

Particular state and local government pension issues can be explained by a general economic model of the demand for and the supply of state and local government pensions.

The theoretical model will specify the wage and pension elements of compensation, the demand for pensions, and the rate of substitution between wages and pensions.

\*See Appendix A for a key to the section of the research design which addresses the research questions outlined in the Request for Grant Applications.

Employees earn income (Y) which represents current consumption ( $C_0$ ), current savings ( $S_0$ ), and future consumption ( $C_1$ ) in the form of pensions. The allocation between current and future consumption depends on the utility function.

$$U = U (C_0, C_1)$$

After modifying the wage rate (W) for current and future income tax rates,  $t_0$  and  $t_1$ , the rate of return (r) on savings, and pension benefits (P), consumption is

$$C_0 = (1-t_0) W - S_0$$

$$C_1 = S_0 + (1 - t_1) (r S_0 + P).$$

Utility maximization techniques will be used in order to identify the optimal pension (P) level.

Employers view pensions as a component of total labor costs.

$$a = \Phi + w$$

where

a = labor cost

$\Phi$  = pension cost or premium

w = wage

and  $\frac{\partial w}{\partial \Phi} \equiv w\Phi < 0$

Labor cost will be incorporated in a production function of government services in order to evaluate cost-minimization conditions. One second-order condition for cost minimization is

$$w_{\Phi\Phi} = \frac{\partial^2 w}{\partial \Phi^2} > 0$$

which implies a diminishing marginal rate of substitution between wages and pensions and that an optimum pension level exists from the employee's viewpoint.

In contrast, the employer may be indifferent to the level of pension benefits and sensitive only to the total labor cost. If the total cost of labor remains constant, at a cost of  $(w + \Phi)$  and employers pay the cost of pensions as those costs are incurred, then employers will be indifferent as to whether all, some, or none of total labor costs are paid in the form of pension benefits.

The model will also suggest that there is a positive relationship between pensions and changes in real income.

The salaries and pension benefits of policemen will be subjected to both cross-sectional (necessary data is already in possession of Program Planners, Inc.) and time series analysis in order to test the substitution and real income hypotheses.

Equilibrium conditions will be the basis for analysis of the following issues:

- 1) the rate of substitution between labor and capital. To the extent that the cost of labor increases such that the value of the marginal product of capital (VMPK) exceeds the value of the marginal product of labor (VMPL), there will be a transfer of labor to capital. It is expected that the time-series analysis referred to earlier will reveal that the pension portion of labor costs has increased. However, the relevant variable in evaluating capital - labor ratios is the total labor cost, and not the pension component alone. If VMPL is greater than VMPK, even though the pension portion of labor costs is relatively high, there will be a transfer to labor from capital. Expenditure data for a sample of state and local governments will be subjected to time series regression analysis in order to identify the elasticity of the capital - labor ratio with respect to labor costs and with respect to the pension component of labor costs. The sample will include expenditures for common municipal functions, as defined by the Bureau of the Census, for the thirty-two largest cities and

for education employees in the thirty largest states. These data have already been accumulated by Program Planners, Inc. for other purposes. The uniformity of services provided by municipalities and education departments will improve the confidence level of statistical inferences.

2) distribution effects. The economic model defines pensions as deferred compensation and, as a consequence, as income earned. Pensions are a portion of the cost of labor inputs and are not grants, subsidies, or gratuities. The model demonstrates a trade-off or substitution between pensions and wages and there is no basis for the conclusion that income is redistributed where a group of employees earn pension benefits and that there is no income redistribution where a group of employees do not earn pension benefits. The model will also include the alternatives available to governments in terms of paying for, or funding, pension benefits. The wealth transfers associated with various levels of pension funding will be illustrated in a fashion similar to the following matrix where adequacy is defined as paying pension costs as they are incurred.

LEVEL OF PENSION FUNDING

Wealth Effect On	Less than Adequate	Adequate	More than Adequate
Current Generation	Gain	None	Lose
Future Generation	Lose	None	Gain

The economic model will be developed simultaneously with the beginning of the research that will comprise Stages I, II, and III.

I. The Issue Of Pension Funding

In deferring the promulgation of standards for state and local government pension funds, P.L. 93-406 called for a study of various aspects of such funds. A Pension Task Force (P.T.F.) was established by the Labor Standards Subcommittee of the House Committee on

Education and Labor for the purpose of conducting the study of state and local government pension funds.

During the past two and one-half years, the P.T.F. has performed an unprecedented survey of the more than 6,000 state and local government pension funds and will soon issue a report of its survey results and conclusions.

The relevance of the P.T.F. survey to the issue of pension funding is the data obtained by the P.T.F. from the state and local government pension funds concerning levels of funding. An extensive questionnaire dealing with, among other issues, benefit levels and financing was completed by more than 90% of all state and local government pension plans.

Although the P.T.F. report will discuss financing on an aggregated basis (by size of pension plan membership) the data can be disaggregated in order to evaluate particular pension plans. The correlation of P.T.F. pension plan data with widely available governmental expenditure<sup>a</sup> data will be the basis for a series of analyses for a selected subset of the universe of the state and local government pension plans.

The subset with which this analysis will be concerned is:

- 1) all state governments, individually and summed,
- 2) municipal governments serving populations of 300,000 or more persons, individually and summed,
- 3) the sum of (1) and (2).

The pension cost of plan sponsors will be reported as a proportion of expenditures and will be analyzed on the basis of:

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- a. Program Planners, Inc. prepares annually a series of 176 tables of data in two volumes, much of which deals with revenue and expenditure levels of state and local governments. With few exceptions, either or both expenditure and pension financial data will be aggregated because of the participation by more than one political subdivision in a pension plan, or, because the employees of a particular political subdivision may be members of different pension plans.

- 1) current funding schedules,
- 2) funding schedules sufficient to finance the normal cost,
- 3) funding schedules sufficient to finance the normal cost plus interest on unfunded accrued liabilities, and
- 4) funding schedules sufficient to finance the normal cost plus the amortization of unfunded accrued liabilities over a 40-year period, the maximum period of amortization permitted in private sector pension funds.

These data will serve as indicators of the cost of government and levels of compliance under various funding standards, and as the basis for estimates, using actuarial methods, of future costs.

Additionally, the relative level of funding, or depth of funding, will be illustrated by developing a series of ratios which have, in the past, been adopted and used by the Shinn Commission, the Pension Task Force, and recommended for use by the American Institute of Certified Public Accountants in its Generally Accepted Accounting Principles.

A general actuarial model will be specified which explains the factors that affect pension costs. The actuarial model will describe, for example, the cost implications to employers and employees associated with: a reduction or an increase in the normal retirement age or benefit formulas; a change in the funding schedule between any two levels on the spectrum running from pay-as-you-go to full actuarial reserve funding; the effect of general price inflation; and the relative effects of changes which are made either retroactively or prospectively.

The general actuarial model will also be used to explain the importance of the assumptions that are used in the valuation of pension costs. The relative importance of the following assumptions will be expressed in terms of the influence that each assumption exerts on the total pension cost:

1. Mortality rates
2. Vesting
3. Turnover
4. Age(s) of Retirement
5. Disability Benefit
  - a. job-connected
  - b. not job-connected
6. Death Benefit
  - a. job-connected
  - b. not job-connected
7. Post-retirement Death Benefit
8. Rate of Future Salary Changes
9. Return on Assets
  - a. on active member reserves
  - b. on retiree reserves

The general actuarial model, in an abbreviated and simplified form, is:

$$[P_s] \times [A + B - C - C^* - D - E] \times [F_s] = R_s$$

$$[P_d] \times [D] \times [F_d] = R_d$$

$$[P_{C^*}] \times [C^*] \times [F_{C^*}] = R_{C^*}$$

$$[P_e] \times [E] \times [F_e] = R_e$$

$$R_s + R_d + R_{C^*} + R_e = AL$$

Where:

$P_s$  = normal pension benefit

$C$  = non-vested terminations

$P_d$  = disability benefit

$C^*$  = vested terminations

$P_{C^*}$  = vested benefit

$D$  = disability terminations

$P_e$  = death benefit

$E$  = death terminations

$A$  = initial population

$F_s$  = discounted annuity value of  $P_s$

$B$  = new entrants

$F_d$  = discounted annuity value of  $P_d$        $R_d$  = reserve for disability benefit

$F_{C*}$  = discounted annuity value of  $P_{C*}$        $R_{C*}$  = reserve for vesting benefit

$F_e$  = discounted present value of  $P_e$        $R_e$  = reserve for death benefit

$R_s$  = reserve for normal pension benefit      AL = accrued liabilities

The power exerted by these assumptions will be illustrated by a series of actuarial valuations of a hypothetical pension fund membership.

The general actuarial model will be used to define and quantify the effect of changes in the actuarial assumptions employed in the valuation of pension fund liabilities. For example, the interest assumptions and the salary progression scales used in the valuation of liabilities will be altered independently and jointly in order to demonstrate their effect on accrued liabilities.

The model will also be used to explore the merits of actuarial funding versus pay-as-you-go funding under conditions of relatively high price inflation over extended periods of time. Under conditions of protracted price inflation at relatively high rates, actuarial funding requires governments to pay pension costs with dollars that will have a sharply diminished value in future years when pensions become due. Under such conditions, appropriate actuarial assumptions may result in pension costs that equal or exceed the cost of wages or payrolls. Hyper-inflation explains, in good part, the virtual extinction of actuarially reserved pension plans in South American countries.

The model will be used in an attempt to identify the range of price inflation which suggests that pay-as-you-go funding is preferable to actuarial funding.

The general actuarial model and the specific state and local government expenditure and pension data will be integrated in order to suggest the results of specific

changes in: pension benefit levels, funding levels, vesting criteria, expansions or contractions in work-forces, etc. and the impact of those results on the cost of pensions to governments and to their employees.

The specification of the general economic model and the general actuarial model along with the investigation of expected fiscal and efficiency implications of changes in various components of the pension agreement will constitute the first stage of the research.

## II. Asset Management

Asset management, or the investment of the monies that represent the reserves of pension funds, has, in few places, been more regulated or later in developing than in state and local government pension funds. The studied efforts of state and local governments to ensure the safety of funds led to restrictions on the types of investments that could be made with pension fund assets and were limited generally to U.S. Government securities, to utility bonds, to high-grade corporate bonds. More recently, at times varying with each pension plan, mortgages and equity issues have become acceptable investment instruments.

Asset management requires the investment agent to select the mix of securities which optimizes rate of return and risk. The sensitivity of rates of return in both equity and debt markets to business cycles and the relatively random nature of the business cycle over the long term implies that optimality changes over time.

The fact that the trade-off between risk and rate of return is difficult to make at any particular point in time is complicated by the full knowledge that the parameters of the trade-off will change at some time in the future.

In order to identify the optimal investment mix, the economic and actuarial models will be used to isolate the long-term investment goal of state and local government pension funds.

The rates of returns for commonly accepted investment vehicles will be evaluated for the past thirty years using three-year, five-year, and ten-year rolling averages.

A hypothetical rate of return will be calculated for the past thirty years which assumes that no more than a fixed portion of assets can be reinvested in a different investment vehicle each year and that investment decisions are made on the basis of the rates of return yielding in the preceding year. The hypothetical rate of returns will be a useful tool for asset managers in evaluating the results in their own portfolios.

The ability of pension fund asset managers to achieve hypothetical rates of returns will be examined in the context of legal constraints, custom and tradition, and the relationship between the pension funds and state and local governments. Case histories of a small sample of pension plans will be used to identify the apparent results of such constraints.

The investment performance of the sample of pension funds will be compared to the investment results of pooled investment accounts of major insurance companies and commercial banks, and the higher or lower performance of state and local governments will be translated into additional costs or savings to state and local governments.

The issues of wealth transfer and income distributions via the investment program will be addressed in terms of investments in human resource development, and in central city mortgages. In either instance, the existence of unmet demand represents a market failure.

Because the risk associated with many of these types of investments is high, the adherence to standards of fiduciary responsibility precludes the making of such investments.

Through the use of the general economic model and the trade-off between risk and rate of return, the wealth

and distribution effects of investments for socially desirable purposes will be specified.

The experience of New York City pension funds during the past three and one-half years will be used as a case study.

During the past three and one-half years, New York City pension funds have purchased \$3.3 billions of New York City bonds. This amount, equivalent to 30% of their total assets, far exceeds the portion of assets that private pension plans can invest in the securities of their employers.

The basis for the decision by the New York City pension funds to invest more than \$3 billion in New York City bonds will be reviewed in the context of the following issues:

- 1) risk,
- 2) rate of return,
- 3) fiduciary responsibility, and
- 4) social welfare.

The case study will reveal the coalescence of interests that led to the pension fund investment agreement in order to develop criteria for decision - making with regard to other types of socially desirable investments.

Incentive schemes will be designed for the purpose of altering the risk and rate of return from socially desirable investments and to qualify such investments as acceptable under standards of fiduciary responsibility, prudent man, etc.

The conclusions reached in the historic and comparative analyses, along with reasonable projections of the program to develop incentives for socially desirable investments, will be evaluated in terms of expected future investment results and portfolio analysis will be employed to estimate the results of various future investment programs. The conclusions concerning past, present and future asset management practices and policies will constitute the second stage of the research.

### III. Compensation Levels

With the exception of the Shinn Commission's comparison of pension benefits between New York City and private sector corporate employees, there has been no rigorous analysis of pension benefit comparability.

This research will evaluate pension benefits for both public and private sector employees. To the extent possible, two pension levels will be evaluated.

The first approach will be to estimate the value of pension benefits to employees on the basis of current salaries and pension benefit formulae. The method used will be to calculate the present value of pension benefits that will be paid during the lifetime of retirees and converting that present value into a single annual premium payable during each year of employment preceding retirement. The single annual premium will represent the value of pension benefits to employees on a current basis, and, when added to the current wage level along with the value of non-wage, non-pension fringe benefits, will comprise compensation.

The second approach will be to estimate the cost of employee pension benefits on the basis of the most recent employer and employee contribution rates to pension funds.

The analysis of compensation will be limited to current wage levels, current pension levels, and the value of health and insurance related benefits. Compensation data will be adjusted to exclude the effects of inter-regional price levels and price inflation.

Compensation data will be analyzed on the basis of:

- 1) the average compensation of all employees of the selected municipal and state governments,
- 2) within municipal governments, the average compensation of:
  - a) policemen,
  - b) firefighters,
  - c) supervising clerks,
  - d) accounting clerks, and,
  - e) computer operators.

- 3) within state governments, the average compensation of:
  - a) teacher
  - b) policeman, state trooper, highway patrolman, etc;
  - c) corrections officer, prison guard, etc., and,
  - d) mental health or hospital nursing aide.

Program Planners, Inc. currently conducts annual surveys of compensation for the five occupation groups shown above under municipal governments. The table on the following page illustrates the compensation data for policemen in descending rank, after adjustment for inter-regional differences in price levels.

The adjustment for inter-regional differences in price levels is a technique employed originally by Program Planners, Inc. in 1970 in order to present wage and compensation data on a uniform basis. The price adjustment reveals the purchasing power of wages and compensation and thereby identifies those areas where wages and compensation may appear to be low but, because of even lower price levels, those wages and compensation will have a relatively high level of purchasing power.

Private sector compensation data will be accumulated in an identical fashion for firms in service industries and firms which perform services which are similar in nature to services performed by state and local governments.

In estimating the pension component of compensation, aspects of pension benefits, which are sophisticated or often overlooked by other researchers, will be fully articulated and entered into the benefit calculations. For example, some pension plans provide that a retiree will receive a benefit during his lifetime and, after his death, a portion or all of that benefit is paid to his beneficiary for their lifetime. A second example is the payment of post-retirement cost-of-living increases.



TABLE 1: RANKING OF MAJOR UNITED STATES CITIES BY ADJUSTED  
TOTAL ANNUAL COMPENSATION OF A POLICE OFFICER, MAY 1978

Rank	City	Annual Wage	Employer Pension Contribution	Employer Health & Related Benefits Cost	Total Annual Compensation	Inter-regional Price Adjustment Factor		Adjusted Total Annual Compensation
						Price Adjustment Factor	Inter-regional Price Adjustment Factor	
1	Los Angeles	\$20,348	\$10,011	\$ 803	\$31,162	1.0012	1.0012	\$31,125
2	San Francisco	19,098	14,113	390	33,601	1.0826	1.0826	31,037
3	Detroit	19,172	10,318	1,108	30,598	1.0188	1.0188	30,033
4	Seattle	18,691	8,686	1,022	28,399	1.0061	1.0061	28,227
5	Washington	19,871	8,381	644	28,896	1.0538	1.0538	27,421
6	Houston	17,061	4,606	387	22,054	0.9054	0.9054	24,358
7	Minneapolis	18,108	5,795	854	24,757	1.0413	1.0413	23,775
8	New York City	18,781	8,115	844	27,740	1.1675	1.1675	23,760
9	Chicago	19,236	3,411	843	23,490	1.0131	1.0131	23,186
10	San Jose	19,284	4,489	820	24,593	1.0826	1.0826	22,717

(Note: See Appendix B for methodology and sources.)

Where pension payments are continued to a beneficiary after the death of a retiree or where cost-of-living adjustments are routinely paid, the straightforward calculation of pension benefits does not reveal the full, ultimate value of pension benefits. To illustrate, the normal retirement benefits of policemen in New York City, Los Angeles and Washington D.C. are shown below on the basis of pension payable at retirement (assuming current salary levels and benefit formulae) along with the average annual value of the pension during the expected lifetime of retirees.

Pension Benefit of Policemen

<u>Employer</u>	<u>At the time of Retirement</u>	Value of average annual benefit after adjusting for continuation of payments to beneficiaries & cost-of-living adjustments
New York City	\$10,358	\$10,358
Washington D.C.	12,598	21,779
Los Angeles	11,191	23,005

(Note: See Appendix C for methodology.)

The adequacy of pension and Social Security benefits will be viewed in terms of:

- 1) the replacement or continuation of pre-retirement income levels;
- 2) the methods, if any, by which post-retirement adjustments in pensions are made to reflect price inflation;
- 3) the demographic characteristics of retirees; and,
- 4) standard measurements of income required during retirement.

On the basis of pension benefit formulas accumulated by the P.T.F. and pension and salary data compiled or to be compiled by Program Planners, Inc., the pension benefits of state and local government and private sector employees will be computed. The pension

benefits available will be depicted as a percentage of pre-retirement income. Selected public and private sector pension benefits will be illustrated on a remaining-lifetime basis, i.e. retirement income, composed of pension and Social Security benefits, will be estimated currently and projected for each year of the retiree's expected life in order to quantify the value of automatic cost-of-living adjustments in pension and Social Security benefits and to estimate the degree by which retirement income exceeds, equals or lags behind the rate of price inflation.

The demographic characteristics of retirees will be examined in order to identify changing consumption patterns. Changes in family size, age of family members, geographic location, and increased leisure time will result in reallocations of income from housing and clothing to medical care, recreation and transportation.

Budgets for retired persons were developed and are maintained by the Bureau of Labor Statistics (B.L.S.) of the U.S. Department of Labor.

The components of the B.L.S. budgets, designed to reflect a lower, an intermediate, and a higher standard of living, were last updated in 1961. Between 1961 and 1967 each element of the budgets was priced directly and since 1969 has not monitored actual price changes, but has, instead, estimated price changes on the basis of aggregate price changes in major categories of expenditure.

The relatively obsolete nature of the B.L.S. budgets renders them of little use in gauging the effectiveness of retirement income in sustaining a given standard of living.

In order to estimate the adequacy of retirement income, without regard to fixed or given standards of living, pre- and post-retirement needs will be studied in order to isolate expected changes in consumption patterns, in the context of smaller family size,

migration, increased leisure time and increased ability of the retiree to perform services that might otherwise be purchased.

The result of the analysis of pre- and post-retirement needs and consumption patterns will be a set of estimates, as a function of the level of pre-retirement income, of the income required in retirement in order to sustain a constant standard of living.

The survey of current levels of public and private sector pension benefits and total compensation, the illustration of post-retirement income streams, and the formulation of criteria for estimating the retirement income required to sustain a constant standard of living will constitute the third stage of the research.

#### IV. The Future of State & Local Government Pensions

Research of levels of pension funding and benefits, asset management, and benefit adequacy will have defined the issues which face state and local governments and their employees.

The future of state and local government pensions will be determined by:

- 1) the rate of change in the levels of pension benefits provided to employees,
- 2) the rate of change in the employee population,
- 3) the rate of change in funding levels,
- 4) the rate of change in asset management performance, and,
- 5) the rate of change in resources available to state and local governments.

The future events or developments in state and local government pension plans will, in turn, cause changes in the rates of pension plan asset accumulations which will lead to changes in the rate of investment in the national economy.

Endogenous and exogenous changes in state and local government pensions will be projected for the purpose of estimating effects on employees, governments, government constituencies, local economies and the national economy.

Forecasting techniques will be used to estimate the independent and joint effects of:

<u>Events Leading to Increased Pension Costs</u>	<u>Events Leading to Decreased Pension Costs</u>
<ul style="list-style-type: none"><li>- Increased demand for pensions<ul style="list-style-type: none"><li>• reduction in retirement age</li><li>• improvement in pension formula</li><li>• new or improved post-retirement pension adjustments</li><li>• increased scope of benefits</li></ul></li><li>- Deteriorating asset management</li><li>- Federal standards similar to E.R.I.S.A.</li></ul>	<ul style="list-style-type: none"><li>- Reductions in pension benefits<ul style="list-style-type: none"><li>• across-the-board reductions</li><li>• reductions for future employees</li></ul></li><li>- Limitation on resources<ul style="list-style-type: none"><li>• Proposition 13 and similar actions</li><li>• reduction in Federal grants and assistance</li><li>• declining economic activity</li></ul></li><li>- Improved asset management</li></ul>

The local, regional and national economic implications of these various events will be quantified, or the direction of change and the magnitude of change will be estimated.

The estimates of effects of various policy modifications will constitute the final stage of the research.

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STAFFING PROPOSAL

Mr. Jack Bigel will be the Project Director and, thus, have overall responsibility for the successful completion of the research study.

Mr. Anthony Gajda will be the Assistant Project Director and the Principal Investigator and will serve as the liaison between Program Planners, Inc. and the Department of Housing and Urban Development. The Assistant Project Director's responsibilities will include the organization and coordination of all project tasks and the preparation of all progress reports. As the Economist for the study, Mr. Gajda will develop the economic model and conduct all economic analyses. In addition, Mr. Gajda will have primary responsibility for the preparation of the final report.

The project directors will be assisted by Mr. Max Weinstein and Mr. Allen Brawer. Mr. Weinstein, an actuary, will be responsible for the development of an actuarial model and all actuarial analyses, valuations and comparisons. The project's attorney and accountatn will be Mr. Brawer, whose efforts will be concentrated in the area of governmental expenditures and the evaluation of pension agreements.

The interdisciplinary nature of the proposed research study will require the expertise and talents of the entire PPI project staff during each phase of the research.

In addition to the PPI project staff, consultants will be utilized during various phases of the study. A consultant will be retained to assist in the Asset Management stage of the project. This consultant's expertise will be in the areas of investments and portfolio analysis.

Program Planners, Inc. will also contract with a consultant experienced in economic theory and analysis.

The project staff and the consultants will be assisted by the PPI Research Department staff. The research staff will be responsible for the collection of all necessary data during the four stages of the study. Clerical support will be provided by PPI staff.

CHART 1: MANAGEMENT PLAN BY TASK, MILESTONES, AND PRODUCTS

	Month from Start																							
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24
Project Start-up																								
• meet with project officer																								
Work Program Revisions																								
Design of Sample																								
• identify state and local government pension funds to be analyzed																								
• identify private sector plans to be used for comparison levels comparison																								
I Level of Funding																								
- Formulation of economic model																								
- Actuarial model																								
• refinement of model																								
• computer programming & testing																								
• construction of hypothetical population																								
• conduct of actuarial valuations																								
- Data collection																								
• from P.T.F.																								
• Gov't. expenditure data																								

CHART 1: Continued

	Month from Start																							
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24
- Analysis of data																								
• compute depth-of-funding measures																								
• compute pension costs at various degrees of funding																								
• evaluate future effects of various funding standards																								
• evaluate $\Phi/\alpha$																								
• evaluate capital - labor ratios																								
• evaluate influence of actuarial assumptions on pension costs																								
- Report																								
• Preliminary Draft																								
• Final Draft																								
II Asset Management																								
- Define investment goals																								
- Data Collection																								
• 30-year history of rates of return																								
• pension fund rates of return																								
• legal and other restrictions																								
• bank & insurance company rates of return																								

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Program Planners, Inc.

CHART 1: Continued

	Month from Start																							
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24
- Data Analysis																								
• develop hypothetical rate of return																								
• evaluate pension fund rates of return with hypothetical rate																								
• isolation of effects of legal & other restrictions																								
• x x x x																								
- Socially - desirable investments																								
• evaluate risk, rate of return, & wealth considerations																								
• case history of New York City pension funds																								
• design incentives for investments for socially-desirable purposes.																								
- Report																								
• preliminary draft																								
• final draft																								
III Compensation Levels																								
- Data collection																								
• pension benefits																								
• total compensation																								
• retiree demographics																								



CHART 1: Continued

	Month from Start																							
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24
- Data Analysis																								
• pension and total compensation comparisons																								
• remaining life-time pension illustrations																								
• pre- and post-retirement expenditure patterns																								
- Develop criteria for estimating retirement income requirements																								
- Report																								
• preliminary draft																								
• final draft																								
IV Future of State & Local Govt. Pensions																								
- Analysis of the effect of policy modifications on pension plans																								
- Report																								
• preliminary draft																								
• final draft																								
Submit Final Report to HUD																								
Submit Progress Reports to HUD																								

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ORGANIZATION AND STAFF QUALIFICATIONS

Program Planners, Inc. is a consulting firm providing services to both the public and private sectors in the areas of pensions, insurance, research, benefit administration and electronic data processing. The PPI staff includes economists, actuaries, health benefit specialists, urban planners, sociologists, health economists, accountants, attorneys, urban geographers, labor economists, and labor relations experts.

The consulting services provided by Program Planners, Inc. which contribute to the firm's qualifications to conduct the proposed research study may be summarized in the areas of Pension and Research.

Pension

The Pension Department of Program Planners, Inc. provides a wide range of services related to the administration of pension plans. PPI designs fixed benefit and fixed contribution plans, performs actuarial valuations and prepares required filings for its clients.

In addition to the routine services provided as consultants to pension plans, PPI also conducts special research projects on benefit, cost, and funding comparisons and evaluations of alternative funding methods and actuarial assumptions of proposed pension plans.

Specifically, Program Planners has completed the following projects:

- An analysis of funding, assumptions, portfolio composition, benefit structure and retirement experience of public employee pension benefits in twenty-five large cities. This study was prepared for the New York City Municipal Labor Committee, June 24, 1976.

- The management of a project in a large public employee retirement system incorporating the redesign of work systems and a personnel system; the introduction of computer technology; the design of information materials and the initiation and supervision of formal training programs;
- The complete development and implementation of a pension plan for Federal employees of a foreign country.

#### Research

The research activities of Program Planners, Inc. include special research studies and surveys for clients as well as basic research projects in new or developing areas related to our consulting services. The full-time professional research staff activities are supplemented by the contacts maintained with experts in a myriad of areas and disciplines. PPI also maintains liaison with educational institutions, private research centers and various professional business and industrial associations. The firm has its own library with a collection of over 4,000 books, reports and periodicals and 823 vertical files for research. The PPI library is affiliated with the New York Regional Urban Information Network (URBIN), the New York Regional Library Association, and is a member of the Special Libraries Association.

The following studies and surveys completed by PPI illustrates the broad scope of our research activities.

- An economic impact analysis of New York City fire safety laws.
- An analysis of the occupational effects of noise and heat, including a survey of the literature and recent developments in applied research.
- An analysis of governmental structure in London, England as a model for New York City.

- An evaluation of a Federal emergency jobs program as an alternative to a Federal income tax rebate.
- An "almanac" of municipal data focusing on the demographics, economics, and fiscal situation of major US cities.

PRODUCT DESCRIPTIONS AND DATES OF SUBMISSION

The research study is to be completed in four stages. At the completion of each stage of research, a comprehensive report will be prepared and submitted to the Department of Housing and Urban Development. The following describes the four reports and lists the expected submission date for each report.

<u>Product Description</u>	<u>Date of Submission</u>
I. Level of Funding - Report  The report will outline the results of the first stage of research. Included in the report will be a description of the economic model, the actuarial model and the analyses of the P.T.P. and governmental expenditure data in regard to pension funding.	18 months from start of project
II. Asset Management - Report  The report will include the hypothetical rate of return developed for pension funds and an evaluation of actual pension fund rates of return with the hypothetical rate. Also included will be the analysis of investments for socially desirable purposes, a case study of NYC pension funds and incentives for socially desirable investments.	13 months from start of project
III. Compensation Levels - Report  The results of the survey of current levels of public and private pension benefits and total compensation will be reported. Criteria developed for estimating retirement income requirements will be contained in the report.	20 months from start of project

IV. Future of State and Local Govt. Pensions 24 months from  
start of project

This report will constitute the final project report. It will contain an analysis of the effect of policy modifications on pension plans and integrate and summarize the findings and results of the previous three stages of research.

In addition to the above reports, Progress Reports will be submitted quarterly to HUD.

BUDGET BY TASKI Level of Funding

- Formulation of economic model	\$19,838
- Actuarial model	69,936
- Data collection	10,677
- Data analysis	27,783
- Report	<u>8,808</u>
	\$137,042

II Asset Management

- Define investment goals	\$ 2,832
- Data collection	6,810
- Data analysis	12,421
- Socially-desirable investments	11,698
- Report	<u>8,122</u>
	\$ 41,883

III Compensation Levels

- Data collection	\$13,918
- Data analysis	26,076
- Criteria for estimating retirement income requirements	15,646
- Report	<u>16,932</u>
	\$ 72,572

IV Future of State & Local Government Pension Plans

- Analysis of effects of policy changes	\$44,553
- Final Report	<u>26,325</u>

**TOTAL PROJECT**

	\$ 70,878
	<u>\$322,374</u>

BUDGET BY EXPENDITURE CATEGORY

Salaries and wages	\$161,755
Fringe benefits	33,166
Permanent equipment	<u>—</u>
Other equipment	2,500
Computer costs	77,500
General overhead expense	40,703
Travel	<u>6,750</u>
	\$322,374

CURRICULUM VITAE

Anthony Gajda

EDUCATION    B.A., Economics, Queens College, CUNY, 1970  
                  M.A., Economics, Hunter College, CUNY, 1975  
                  Ph.D. Candidate, Economics, Graduate School,  
                  CUNY, 1980 (estimated)

PROFESSIONAL EXPERIENCE

1967 - Present    Vice-President and Economist  
                         Program Planners, Inc.  
                         New York, New York

Consultant to municipal and private labor unions, union and corporate pension funds, and union health and welfare funds. Responsible for the supervision of PPI's Pension Department, Health Insurance Department and Data Processing Department. Responsible for all municipal data analyses, employee benefit analyses and comparisons, and various economic research studies and projects undertaken by PPI.

1965 - 1967    Analyst  
                         Group Health, Inc.  
                         New York, New York

PROJECTS AND STUDIES RELATED TO PENSION ISSUES

1975 - 1976    Member, Shinn Commission Task Force  
                         Task Force commissioned by the Mayor of the City of New York to conduct a thorough study focusing on a realistic evaluation of the required City contribution toward funding the five basic NYC pension systems.

1976            "An Analysis of Public Employee Compensation Levels", Project Director  
                         Report prepared for the New York City Municipal Labor Committee which included comparisons of wages, health insurance and pension costs of municipal employees in the 25 largest U.S. cities; a comparison

of levels of total compensation with large private sector corporations; and an analysis of funding, assumptions, portfolio composition, benefit structure and retirement experience of public employee pension benefits in 25 large cities.

1976                    "Analysis of the Report of the Permanent Commission on Public Employee Pension and Retirement Systems." Report prepared for the Municipal Labor Committee, City of New York, March 22, 1976.

1975                    "A Survey of Municipal Employees' Pension Benefits." Assisted in the preparation of the report which was prepared for The New York Conference of Public Employee Organizations. July 3, 1975

1973                    "An Analysis of the Recommendations of the New York State Permanent Commission on Public Employee Pension and Retirement Systems (A4159, and S3435): Their Impact on the Public Service." Report prepared for the New York State Conference of Public Employee Organizations, February 28, 1973.

CURRICULUM VITAE

Max S. Weinstein

EDUCATION B.S., Electrical Engineering, The Cooper Union, 1928

PROFESSIONAL EXPERIENCE

1967 - Present	Program Planners, Inc. New York, New York	Chief Actuary
1967 - Present	Plumbers Union Local 7 Albany, New York	Actuary
1944-1967	New York State Employees' Retirement System Albany, New York	Chief Actuary
1930-1944	State of New York Insurance Department New York, New York	Senior Examiner
1926-1930	State of New York Insurance Department New York, New York	Audit Clerk

PROFESSIONAL ORGANIZATIONS AND SOCIETIES

Fellow, Society of Actuaries  
Fellow, Conference of Actuaries in Public Practice  
Member, American Academy of Actuaries  
Associate, Casualty Actuarial Society  
Member, American Statistical Association  
Member, Mathematical Association of America  
Member, American Pension Conference  
Enrolled Actuary, No. 1107

PUBLICATIONS

"Mortality and Service Experience of the New York State Employees' Retirement System." General Session in the Proceedings of the Conference of Actuaries in Public Practice, Vol. XVII, 1967-1968.

PROJECTS AND STUDIES RELATED TO PENSION ISSUES

1975-1976

Member, Shinn Commission Task Force

Task Force commissioned by the Mayor of the City of New York to conduct a thorough study focusing on a realistic evaluation of the required City contribution toward funding the 5 basic NYC pension systems.

1963-1964

Member, Committee appointed by the State Comptroller to Study the Changes in the Disability Benefit for the New York State Employees' Retirement System.

1958-1960

Member, Committee appointed by the Governor to Study the Form of a Vesting Benefit for the New York State Employees' Retirement System.

1944

Director, Study of Entire Structure of the New York State Employees' Retirement System, commissioned by the State Comptroller and the Governor. Assisted in rewriting the governing law of the Retirement System and the establishment of its Actuarial Department.

1944-1967

As Chief Actuary of the New York State Employees' Retirement System wrote laws regarding pension benefits which required innumerable appearances and testimony before State legislative committees. Author of the following laws:

- the law instituting changes in the pension benefit systems, in particular, the age 55 retirement benefit. (1964-1966)
- the law which increased take home pay for New York State employees. (1958-1960)
- the law which instituted vesting benefits (1958-1960).
- the law that provided social security benefits to state employees (1953 - 1955).

CURRICULUM VITAE

Allen B. Brawer

EDUCATION

Master of Arts, New School for Social Research,  
Department of Urban Affairs and Policy Analysis,  
1973.

Juris Doctor, Brooklyn Law School, 1969.

Bachelor of Business Administration (accounting),  
Baruch College, City of New York, 1966.

PROFESSIONAL EXPERIENCE

1978 - Present Senior Analyst, Program Planners, Inc.  
New York, New York

Duties include data analyses of municipal financing,  
specifically New York City; legal interpretations of  
financial and collective bargaining agreements. Management  
consultant to the New York City Teachers Retirement System.

1977 - 1978 Special Counsel to Director, New York City  
Office of Management and Budget

Senior advisor to Budget Director on all policy issues, with  
particular emphasis on fiscal and administrative affairs.  
Special projects included: prepared executive order for  
administering budget under revised City Charter; analysis  
of various financial proposals concerning City's debt; de-  
veloped process for agency consultation with community  
boards concerning expense and capital budget.

1976 - 1977 Executive Assistant to Deputy Director,  
New York City Office of Management and Budget

Senior advisor to Deputy Director, with particular emphasis  
on City finances and revenues; coordinated preparation of  
FY 1978 Revenue Budget; designed and implemented FY 1978  
Expense Budget analytic process; responsible for analysis  
of financial matters, specifically Municipal Assistance  
Corporation debt, City debt, and City's cash position; de-  
signed and implemented computerized financial mode for  
New York City, with emphasis on fiscal options; assisted in  
implementation of computer model of Municipal Assistance  
Corporation debt.

1975 - 1976

Senior Financial Analyst, New York City  
Office of Management and Budget

Duties included City and Municipal Assistance Corporation debt projections; analysis and projection of City's cash requirements; responsible for producing monthly City Financial Plan Statements for United States Treasury.

1974 - 1975

Senior Planner, Criminal Justice, New York  
City Office of Management and Budget

Supervised three planners in analysis of New York City criminal justice services; developed and supervised evaluation of Pre-Trial Services Agency; evaluate pre-arrangement processing program, with recommendations for improvement leading to City-wide implementation and annual savings of \$4 million; analyzed juror management in New York City court system and developed new program, with annual savings of \$2 million.

1974 - 1974

Analyst, New York City Energy Office

Developed and implemented New York City gas rationing and allocation plan.

1973 - 1974

Analyst, New York City Fire Department

Responsible for various management analyses including: sick leave, use of emergency vehicles, and response to false alarm.

1969 - 1970

VISTA Lawyer, San Francisco Local  
Development Corporation

Responsible for all legal and financial assistance to minority businessmen.

#### PROFESSIONAL ORGANIZATIONS

Member, New York State Bar Association.

#### PAPERS

Priority Analysis and Resource Allocation In New York City's  
Budgeting Process. University of New York at Stony Brook,  
May 24, 1977.

APPENDIX A

The following key directs the reader to the appropriate section of the proposal in which a particular research question, as outlined in the Request for Grant Applications, is addressed.

	<u>Section</u>	<u>Page Number</u>
I.	Policy Alternatives and Impacts	
	A - Actuarial vs Current Financing	
	A - 1	
	A - 2	
	B - Wealth Distribution	
	C - Comparative Compensation	
	D - Cost of Government	
	E - Portfolio Incentives	
II.	Benefit Issues	
	A - Adequacy	
	B - Comparability	
III.	Funding Issues	
	A - Actuarial Assumptions	
	A - 1	
	A - 2	
	A - 3	
	A - 4	
	A - 5	
	A - 6	
	B - Portfolio Questions	
	B - 1	
	B - 2	
	B - 3	
	C - Definitions of Funding Levels	

APPENDIX B

RANKING OF MAJOR UNITED STATES CITIES BY ADJUSTED  
TOTAL ANNUAL COMPENSATION OF A POLICE OFFICER, MAY 1978

Rank	City	Annual Wage <sup>a</sup>	Employer Pension Contribution <sup>b</sup>	Employer Health & Related Benefits Cost <sup>c</sup>	Total Annual Compensation	Inter-regional Price Adjustment Factor <sup>d</sup>	Adjusted Total Annual Compensation
1.	Los Angeles	\$20,348	\$10,011	\$ 803	\$31,162	1.0012	\$31,125
2.	San Francisco	19,098	14,113	390	33,601	1.0826	31,037
3.	Detroit	19,172 <sup>e</sup>	10,318	1,108	30,598	1.0188	30,033
4.	Seattle	18,691	8,686	1,022	28,399	1.0061	28,227
5.	Washington	19,871	8,381	644	28,896	1.0538	27,421
6.	Houston	27,061	4,606	387	22,054	0.9054	24,358
7.	Minneapolis	18,108	5,795	854	24,757	1.0413	23,775
8.	New York City	18,781 <sup>f</sup>	8,115 <sup>g</sup>	844	27,740	1.1675	23,760
9.	Chicago	19,236	3,411	843	23,490	1.0131	23,186
10.	San Jose	19,284	4,489	820	24,593	1.0826	22,717

NOTES:

- a. Annual wage at maximum grade not including longevity payments.
- b. Includes Social Security payments where applicable.
- c. Health and life insurance, supplemental insurance, dental, optical, drug, and other related plans where applicable. Average employer contribution per employee. In cities with different rates for individual and family coverage, the employee population is weighted by a ratio of 67% family and 33% individual.
- d. Derived by dividing each city's US Bureau of Labor Statistics Intermediate Budget for a Four Person Family, Autumn, 1977, by the US Urban Budget, New York City thus equals 1.1675. For San Jose, San Francisco is used. For other cities without a published budget, the adjustment factor 1.0229 is based on the budget for all US Metro areas.
- e. Expired contract. Fy 1977/78 agreement currently in arbitration.
- f. Consists of a base rate of \$17,458, \$441 "Old COLA" and \$882 "New COLA."
- g. Consists of 37.9% pension contribution on \$17,899 (base rate plus "Old COLA"), \$1,071 FICA and \$261 annuity fund. Full pension funding will eventually raise the percent contribution to 42.8%.

Source: Developed from data gathered by Program Planners, Inc. for the second annual total compensation study. Data are obtained through:

International Personnel Management Association  
US Bureau of Labor Statistics  
Bureau of National Affairs  
Questionnaire responses  
Local newspaper clippings  
Telephone interviews

APPENDIX CPension Benefits

In July and August, 1975, Program Planners, Inc. conducted a survey of pension benefits in nine cities. As a continuation of that analysis the benefits paid to police officers in Los Angeles, New York City and Washington, D.C. will be reconsidered.

In order to compare pension benefits in a particular city, these benefits must be computed using the actual salary histories. Annual salaries for police officers for the period 1973 through 1978 were obtained. Pension benefits were then calculated using the benefit formulae as revealed in the nine cities study. Table I shows these calculations:

Table I: Normal Retirement Allowances  
Based on Actual Salaries

<u>City</u>	<u>Police Officer<sup>a</sup></u>
New York City	\$10,358
Los Angeles	11,191
Washington, D.C.	12,598

Note:

- a. 25 years of service, any age
1. A Survey of Municipal Employee's Pension Benefits; prepared for the New York Conference of Public Employee Organizations by Program Planners, Inc., New York. July, 1975.

Pension benefits paid to police officer retirees outside of New York City increase substantially with the incorporation of two "invisible benefits," not reflected in Table I.

- cost of living adjustment, and
- continuation of benefit payments to beneficiaries.

Los Angeles and Washington, D.C. provide cost-of-living protection for their retirees, tied to the Consumer Price Index. No similar protection is available in New York City except for pre-1968 retirees. Table II shows the average benefit that will be paid during the expected lifetime of the retiree.

Table II: Average Annual Retirement Benefits When Cost-of-Living Escalators are Included in Payments<sup>a</sup>

<u>City</u>	<u>Police Officer<sup>b</sup></u>
New York City	\$10,358
Los Angeles	16,906
Washington, D.C.	19,032

Notes:

- a. Benefits were calculated as the average benefit payable during the future retired lifetime, assuming a future annual rate of inflation of 3%. Retired lifetimes were estimated using Table of Expected Return Multiples, Internal Revenue Code Reg. Sec. 1.72-9
- b. Assumed retirement age: 50

The pension benefit paid in New York City, and illustrated in Tables I and II, is a "life annuity without refund." In contrast the benefits shown in the tables for retirees in Los Angeles and Washington, D.C. provide for continuation of pension income to a beneficiary at the death of the retiree. Table III demonstrates the pension benefits payable if calculated for the life of the retiree alone (life annuity) and incorporating the previously discussed cost-of-living adjustments.

Table III: Average Annual Retirement Benefits with Cost-of-Living Escalators, Adjusted to a Straight Life Annuity Form<sup>a</sup>

<u>City</u>	<u>Police Officer<sup>b</sup></u>
New York City	\$10,358
Los Angeles	23,005
Washington, D.C.	21,779



Program Planners, Inc.

Notes:

a. Adjusted benefits were calculated using Table of Expected Return Multiples, Internal Revenue Code Reg. Sec. 1.72-9. Normal form of benefits paid are as follows:

New York City -- Life Annuity with Refund  
Los Angeles -- Joint and Full Survivor  
Washington, D.C. -- Joint and 40% Survivor

b. Assumed retirement age : 50 Male  
Assumed beneficiary age: 50 Female



Program Planners, Inc.

AUDIT REPORT

This proposal is the first response to a Federal Government solicitation prepared by Program Planners, Inc. For this reason, a Federal Agency certification of audited rates for wages, and indirect costs is not available.

TO: Mr. Jack Bigel  
FROM: Mr. Jonathan Schwartz

DATE: September 27, 1978  
SUBJECT: POLICE AND FIRE VARIABLE  
SUPPLEMENTS FUNDS

---

I. INTRODUCTION -

The Patrolmens' Variable Supplements Fund and the Police Superior Officers' Variable Supplements Fund were established by Chapter 876 of the Laws of 1970. The Firemen's Variable Supplements Fund and the Fire Officers' Variable Supplements Fund were established by Chapter 877 of the Laws of 1970. The following description of their operations will be restricted to the Police Variable Supplements Funds, which function in the same manner as the Fire Funds.

II. DESCRIPTION OF OPERATIONS -

In each fiscal year since 1970, the following procedure has been followed:

- 1) The income to the Police Pension Fund, Article 2 from stock investments (including unrealized gains or losses) is determined.
- 2) The income which could have been realized had the entire stock portfolio been invested in fixed-income securities is estimated.
- 3) If the earnings from stocks (including unrealized gains and losses) exceed the potential fixed-income earnings, such excess is transferred (skimmed off) from the Police Pension fund to the Police Variable Supplements Funds.
- 4) If the potential fixed-income earnings exceed stock earnings, then a loss is incurred which must be made up before any funds are transferred from the Pension Fund to the Variable Supplements Funds.

**III HISTORY OF INVESTMENT EXPERIENCE -**

<u>FISCAL YEAR</u>	<u>STOCK EARNINGS</u>	<u>FIXED-INCOME HYPOTHETICAL EARNINGS</u>	<u>(2) - (3) SKIM - OFF</u>
(1)	(2)	(3)	(4)
1970	- \$ 9.6 million	\$ 2.4 million	- \$12.0 million
1971	25.1	4.8	20.3
1972	29.8	14.6	15.2
1973	- 21.1	21.5	- 42.6
1974	- 48.2	- 25.3	- 73.5

Precise figures are not available for any subsequent fiscal years with respect to the Police Variable Supplements Funds. However, since stock earnings of the Fire Department Pension Fund did not exceed fixed-income hypothetical earnings in both fiscal 1975 and 1976, it seems reasonable to assume that there was no dramatic movement in the Police Pension Fund's stock portfolio in those years. Furthermore, since (a) very high interest rates have been available in fixed-income securities since 1976, and (b) there was no dramatic overall improvement in the stock market between July 1, 1976 and June 30, 1978, it also seems reasonable to assume that no significant "skim-off" emerged in either fiscal 1977 or 1978.

Consequently, the following conclusions may be drawn from the data shown above:

- 1) A "skim-off" of \$8.3 million (\$20.3 million less \$12.0 million) was transferred to the Police Variable Supplements Funds on account of favorable experience in fiscal 1971.
- 2) A "skim-off" of \$15.2 million was transferred to the Police Variable Supplements Funds on account of favorable experience in fiscal 1972.
- 3) Losses of \$116.1 million (\$42.6 million plus \$73.5 million) emerged in fiscal years 1973 and 1974.
- 4) Investment experience was not particularly favorable between July 1, 1974 and June 30, 1978.

- 5) In order for any further funds to be transferred from the Police Pension Fund to the Police Variable Supplements Funds, a cumulative "skim-off" of at least \$115 million must be accrued, i.e., stock earnings must exceed hypothetical fixed-income earnings by at least \$115 million in the future.

IV. EFFECT OF NOVEMBER, 1975 AGREEMENT

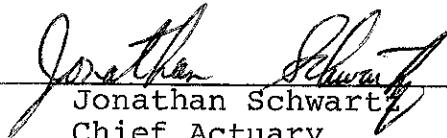
At present, the Police Pension Fund assets include some \$408 million of City-related securities, of which \$360 million was acquired subsequent to July 1, 1975. Had the Police Pension Fund not purchased these securities, most, if not all, of the \$360 million would almost certainly have been invested in stocks. During the negotiations which preceded the November, 1975 agreement, the Trustees of the Police Pension Fund pointed out that if they were to make substantial investments in City-related securities, they would be unable to purchase stocks as had been planned, thereby diminishing the potential for accruing a large "skim-off". Mr. William T. Scott, who was then serving as Third Deputy Comptroller, assured the Trustees that City and MAC securities would be treated as though they were stocks for the purpose of determining Variable Supplements "skim-off", and the Trustees agreed to purchase the City-related securities on the basis of this assurance.

V. POSITION OF INSURANCE DEPARTMENT

The statutes which established the Variable Supplements Funds specified that the New York State Insurance Department has the power to regulate their operations. In its regulatory capacity, the Insurance Department has asserted that since (1) the "skim-off" is based on a comparison of stock earnings and hypothetical fixed-income earnings, and (2) City-related securities are not stocks, it is illegal to take account of City-related securities in determining a "skim-off," regardless of what was agreed to between the Trustees and the Third Deputy Comptroller, Mr. Sam D. Emilia of the PBA took exception to this position of the Insurance Department during a meeting held at DC 37 on September 14, 1978.

VI. SIGNIFICANCE OF DISPUTE -

In point of fact, the aforementioned difference of opinion has little, if any, practical significance. In the latter part of Section III of this memorandum, we demonstrated that the stock investments of the Police Pension Fund would have to generate at least \$115 million of "skim-off" before any additional funds could be transferred from the Police Pension Fund to the Police Variable Supplements Funds. As previously stated, the Police Pension Fund presently holds \$360 million in City-related securities acquired since July 1, 1975, some of which yield as much as 9% per annum. The hypothetical fixed-income yield for fiscal 1976 was 9.2%. Consequently, it is unlikely that any "skim-off" could be generated in 1976 by securities yielding 9%. The hypothetical yield rate for fiscal 1977 and 1978 has not yet been determined. However, if it were to be as high as 9%, it would make absolutely no difference whether or not City-related securities were treated as equities. If the hypothetical fixed-income yield were as low as 8½%, this would result in no more than \$1 million of skim-off in each of fiscal 1977 and fiscal 1978.

  
\_\_\_\_\_  
Jonathan Schwartz  
Chief Actuary

**Value of Assets of the New York City Retirement Systems**  
**As of December 31, 1977**  
**(\$ In Millions)**

**Exhibit A**

<u>Par Value Basis</u>	<u>N.Y.C. Employees</u>	<u>Teachers</u>	<u>Board of Education</u>	<u>Police Article 2</u>	<u>Pire Article 1-B</u>	<u>Total</u>
* New York City Securities (A)	\$ 1423	\$ 1026	\$ 56	\$ 441	\$ 97	\$ 3043
**Corporate and Miscellaneous Bonds	2124	1225	100	534	241	4224
* Mortgages and Real Estate	213	27	—	20	2	262
**Common Stock	553	—	—	345	135	1033
Cash and Short Term Paper	496	177	230	42	954	
<b>Totals</b>	<b>\$ 4809</b>	<b>\$ 2455 (B)</b>	<b>\$ 165 (B)</b>	<b>\$ 1570</b>	<b>\$ 517 (B)</b>	<b>\$ 9516</b>

<u>Market Value Basis</u>	<u>N.Y.C. Employees</u>	<u>Teachers</u>	<u>Board of Education</u>	<u>Police Article 2</u>	<u>Pire Article 1-B</u>	<u>Total</u>
* New York City Securities (A)	\$ 1423	\$ 1026	\$ 56	\$ 441	\$ 97	\$ 3043
**Corporate and Miscellaneous Bonds	1741	972	83	450	201	3447
* Mortgages and Real Estate	213	27	—	20	2	262
**Common Stock	497	—	—	306	117	920
Cash and Short Term Paper	496	177	230	42	954	
<b>Totals</b>	<b>\$ 4370</b>	<b>\$ 2202 (B)</b>	<b>\$ 148 (B)</b>	<b>\$ 1447</b>	<b>\$ 459 (B)</b>	<b>\$ 8626</b>

(A) Includes securities of the Municipal Assistance Corporation and City related agencies  
 (B) Assets held by the Comptroller which excludes holdings of the Variable Annuity Funds.

\* Par Value

\*\* Based on Kuhn Loeb Portfolio Review

\*\*\* Based on Closing Market Prices - 12/31/77

Note: Source of Data - New York City Office of the Comptroller

Summary of New York City Retirement Systems  
Projected Cash Flow - Fiscal Years 1979-1981  
( $\$$  In Millions)

Exhibit B

<u>Receipts</u>	<u>FY 1979</u>	<u>FY 1980</u>	<u>FY 1981</u>	<u>FY 1982</u>	<u>Total</u>
City Contributions					
Employee Contributions	$\$ 1,253$	$\$ 1,325$	$\$ 1,405$	$\$ 1,445$	$\$ 5,428$
Investment Income (1)	$\frac{209}{875}$	$\frac{215}{951}$	$\frac{223}{955}$	$\frac{229}{968}$	$\frac{876}{3,749}$
Total Receipts	$\frac{\$ 2,337}{\$ 2,491}$	$\frac{\$ 2,491}{\$ 2,583}$	$\frac{\$ 2,583}{\$ 2,642}$	$\frac{\$ 2,642}{\$ 10,053}$	
<u>Disbursements</u>					
Pension Payroll	$\$ 901$	$\$ 1,022$	$\$ 1,107$	$\$ 1,192$	$\$ 4,222$
Loans & Excess Contribution	$\frac{126}{163}$	$\frac{127}{91}$	$\frac{127}{91}$	$\frac{127}{91}$	$\frac{507}{436}$
Other					
Total Disbursements	$\frac{\$ 1,190}{\$ 1,240}$	$\frac{\$ 1,240}{\$ 1,325}$	$\frac{\$ 1,325}{\$ 1,410}$	$\frac{\$ 1,410}{\$ 5,165}$	
Excess (Deficiency) of Receipts over Disbursements	$\$ 1,147$	$\$ 1,251$	$\$ 1,258$	$\$ 1,232$	$\$ 4,888$
Less: Investments in Guaranteed Securities Projected in Four Year Financial Plan	$\$ 169$	$\$ 215$	$\$ 258$	$\$ 258$	$\$ 900$
Net Excess (Deficiency) of Receipts over Disbursements	$\frac{\$ 978}{\$ 1,036}$	$\frac{\$ 1,036}{\$ 1,000}$	$\frac{\$ 1,000}{\$ 974}$	$\frac{\$ 974}{\$ 3,988}$	
Beginning Cash Balance	$\$ 1,007$	$\$ 1,985$	$\$ 3,021$	$\$ 4,021$	$\$ 1,007$
Ending Cash Balance	$\$ 1,985$	$\$ 3,021$	$\$ 4,021$	$\$ 4,995$	$\$ 4,995$

(1) Includes both yield on investments and proceeds of maturities.

Source: Office of the Actuary

New York City Retirement Systems  
Projected Cash Flow - Fiscal Year 1979  
 (\$ In Millions)

Exhibit B  
 Page 1

	<u>N.Y.C.</u>	<u>Employees</u>	<u>Teachers</u>	<u>Police</u>	<u>Fire</u>	<u>Board Of</u>	<u>Education</u>	<u>Total</u>
<u>Receipts</u>								
City Contributions		\$ 570	\$ 404	\$ 209	\$ 50	\$ 20	\$1,253	
Employee Contributions		108	48	39	6	8	209	
Investment Income (1)		<u>440</u>	<u>262</u>	<u>118</u>	<u>38</u>	<u>17</u>	<u>875</u>	
<b>Total Receipts</b>		<b><u>\$ 1,118</u></b>	<b><u>\$ 714</u></b>	<b><u>\$ 366</u></b>	<b><u>\$ 94</u></b>	<b><u>\$ 45</u></b>	<b><u>\$2,337</u></b>	
<u>Disbursements</u>								
Pension Payroll		\$ 415	\$ 248	\$ 144	\$ 82	\$ 12	\$ 901	
Loans & Excess Contributions		44	48	25	6	3	126	
Other		<u>126</u>	<u>(2)</u>	<u>24</u>	<u>6</u>	<u>2</u>	<u>5</u>	<u>163</u>
<b>Total Disbursements</b>		<b><u>\$ 585</u></b>	<b><u>\$ 320</u></b>	<b><u>\$ 175</u></b>	<b><u>\$ 90</u></b>	<b><u>\$ 20</u></b>	<b><u>\$1,190</u></b>	
Excess (Deficiency) of Receipts								
Over Disbursements		\$ 533	\$ 394	\$ 191	\$ 4	\$ 25	\$1,147	
Less: Investments in Guaranteed								
Securities Projected in								
Four Year Financial Plan		\$ 80	\$ 53	\$ 26	\$ 7	\$ 3	\$ 169	
Net Excess (Deficiency) of								
Receipts over Disbursements		<u>\$ 453</u>	<u>\$ 341</u>	<u>\$ 165</u>	<u>\$ (3)</u>	<u>\$ 22</u>	<u>\$ 978</u>	
Beginning Cash Balance		\$ 533	\$ 189	\$ 240	\$ 37	\$ 8	\$1,007	(3)
Ending Cash Balance		<u>\$ 986</u>	<u>\$ 530</u>	<u>\$ 405</u>	<u>\$ 34</u>	<u>\$ 30</u>	<u>\$1,985</u>	
(1) Includes both yield on investments and proceeds of maturities.								
(2) Provides for the transfers of reserves to NY State Employees Retirement System for court employees transferred to the State.								
(3) Cash Balance assumes no investment after December 31, 1977 other than the Spring 1978 commitment of \$683 million of New York City Bonds.								

Source: Office of the Actuary.

New York City Retirement Systems  
Projected Cash Flow - Fiscal Year 1980  
(\$ In Millions)

<u>N.Y.C. Employees</u>	<u>Teachers</u>	<u>Police Article-2</u>	<u>Fire Article-1B</u>	<u>Board of Education</u>	<u>Total</u>
<u>Receipts</u>					
City Contributions	\$ 595	\$ 435	\$ 225	\$ 50	\$ 1,325
Employee Contributions	110	50	40	6	215
Investment Income (1)	<u>483</u>	<u>281</u>	<u>134</u>	<u>36</u>	<u>951</u>
<b>Total Receipts</b>	<b>\$ 1,188</b>	<b>\$ 766</b>	<b>\$ 399</b>	<b>\$ 92</b>	<b>\$ 2,491</b>
<u>Disbursements</u>					
Pension Payroll	\$ 486	\$ 268	\$ 159	\$ 92	\$ 1,022
Loans and Excess					
Contributions	45	48	25	6	127
Other	<u>54</u>	<u>24</u>	<u>6</u>	<u>2</u>	<u>91</u>
<b>Total Disbursements</b>	<b>\$ 585</b>	<b>\$ 340</b>	<b>\$ 190</b>	<b>\$ 100</b>	<b>\$ 1,240</b>
Excess (Deficiency) of					
Receipts over Disbursements	\$ 603	\$ 426	\$ 209	\$ (8)	\$ 21
Less: Investments In Guaranteed Securities					
Projected in Four Year Financial Plan	\$ 102	\$ 68	\$ 33	\$ 8	\$ 215
Net Excess (Deficiency) of					
Receipts over Disbursements	<u>\$ 501</u>	<u>\$ 358</u>	<u>\$ 176</u>	<u>\$ (16)</u>	<u>\$ 1,036</u>
Beginning Cash Balance	\$ 986	\$ 530	\$ 405	\$ 34	\$ 1,985
Ending Cash Balance	\$ 1,487	\$ 888	\$ 581	\$ 18	\$ 47
					\$ 3,021

(1) Includes both yield on investments and proceeds of maturities.

New York City Retirement Systems  
Projected Cash Flow - Fiscal Year 1981  
(\$ In Millions)

Exhibit B  
Page 3

<u>Receipts</u>	<u>N.Y.C.</u>	<u>Police</u>	<u>Fire</u>	<u>Board of</u>	<u>Exhibit B</u>
	<u>Employees</u>	<u>Teachers</u>	<u>Article-2</u>	<u>Article-1B</u>	<u>Page 3</u>
City Contributions	\$ 640	\$ 460	\$ 235	\$ 50	\$1,405
Employee Contributions	115	52	41	6	223
Investment Income (1)	492	280	131	35	955
<b>Total Receipts</b>	<b>\$1,247</b>	<b>\$ 792</b>	<b>\$ 407</b>	<b>\$ 91</b>	<b>\$2,583</b>
<u>Disbursements</u>					
Pension Payroll	\$ 531	\$ 293	\$ 174	\$ 92	\$1,107
Loans and Excess Contributions	45	48	25	6	127
Other	54	24	6	2	91
<b>Total Disbursements</b>	<b>\$ 630</b>	<b>\$ 365</b>	<b>\$ 205</b>	<b>\$ 100</b>	<b>\$1,325</b>
Excess (Deficiency) of Receipts Over					
Dishbursements	\$ 617	\$ 427	\$ 202	\$ (9)	\$ 21
Less: Investments In Guaranteed					
Securities Projected in					
Four Year Financial Plan	\$ 122	\$ 82	\$ 40	\$ 9	\$ 258
Net Excess (Deficiency) of Receipts					
Over Dishbursements	\$ 495	\$ 345	\$ 162	\$ (18)	\$ 16
Beginning Cash Balance	\$1,487	\$ 888	\$ 581	\$ 18	\$ 47
Ending Cash Balance	1,982	1,233	743	0	63

(1) Includes both yield on investments and proceeds of maturities.

New York City Retirement Systems  
Projected Cash Flow-Fiscal Year 1982  
(\$ In Millions)

	<u>N.Y.C.</u>	<u>Teachers</u>	<u>Police Article-2</u>	<u>Fire Article-1B</u>	<u>Board of Education</u>	<u>Total</u>
<u>Receipts</u>						
City Contributions	\$ 660	\$ 475	\$ 240	\$ 50	\$ 20	\$ 1,445
Employee Contributions	117	54	42	6	10	229
Investment Income (1)	<u>494</u>	<u>283</u>	<u>136</u>	<u>35</u>	<u>20</u>	<u>968</u>
<b>Total Receipts</b>	<b>\$ 1,271</b>	<b>\$ 812</b>	<b>\$ 418</b>	<b>\$ 91</b>	<b>\$ 50</b>	<b>\$ 2,642</b>
<u>Disbursements</u>						
Pension Payroll	\$ 566	\$ 313	\$ 189	\$ 107	\$ 17	\$ 1,192
Loans and Excess Contributions	45	48	25	6	3	127
Other	<u>54</u>	<u>24</u>	<u>6</u>	<u>2</u>	<u>5</u>	<u>91</u>
<b>Total Disbursements</b>	<b>\$ 665</b>	<b>\$ 385</b>	<b>\$ 220</b>	<b>\$ 115</b>	<b>\$ 25</b>	<b>\$ 1,410</b>
Excess (Deficiency) of Receipts Over Disbursements	\$ 606	\$ 427	\$ 198	\$ (24)	\$ 25	\$ 1,232
<u>Less: Investments of Guaranteed Securities Projected in Four Year Financial Plan</u>						
Net Excess (Deficiency) of Receipts over Disbursements	\$ 484	\$ 345	\$ 158	\$ (33)	\$ 20	\$ 974
Beginning Cash Balance	\$ 1,982	\$ 1,233	\$ 743	\$ 0	\$ 63	\$ 4,021
Ending Cash Balance	\$ 2,466	\$ 1,578	\$ 901	\$ (33)	\$ 83	\$ 4,995

(1) Includes both yield on investments and proceeds of maturities.

SOURCE: Office of the Actuary

Exhibit C

EXAMPLES OF PENSION BENEFITS

New York City Retirement System	Plan	Earnings	Years Of	Percentage	Annual
			Service Credit	Accrual Rate	Retirement Allowance
Employees	A-Career Pension	\$ 17,500	25	55%	\$9,625
	B-Increased-Service-Fraction	\$ 15,000	15	33%	\$4,950
Teacher's Retirement System	A	\$ 22,000	25	59%	\$12,980
	B	\$ 19,000	15	31%	\$5,890
Police	20 Year	\$ 21,000	22	53%	\$11,130
Pire	20 Year	\$ 21,000	22	53%	\$11,130

Note: Retirement allowances for members of the Board of Education Retirement System would be computed in the same manner as for members of the Employees Retirement System.

THE FIVE NEW YORK CITY RETIREMENT SYSTEMS  
PROJECTION OF PURCHASES OF NEW YORK CITY AND MAC SECURITIES  
(FIGURES IN MILLIONS OF DOLLARS)

	Fiscal Year <u>1975-76</u>	Fiscal Year <u>1976-77</u>	Fiscal Year <u>1977-78</u>
<b>Assets -- Beginning of Year</b>	<b>\$7,719</b>	<b>\$8,342</b>	<b>\$9,169</b>
Employer Contributions <sup>1</sup>	\$1,021	\$1,240	\$1,365
Employee Contributions <sup>2</sup>	232	232	232
Investment Income <sup>3</sup>	<u>450</u>	<u>590</u>	<u>691</u>
<b>Total Income</b>	<b><u>1,703</u></b>	<b><u>2,062</u></b>	<b><u>2,288</u></b>
 <b>Benefit and Other Payments<sup>4</sup></b>	 <b><u>1,080</u></b>	 <b><u>623</u></b>	 <b><u>1,350</u></b>
 <b>Net Addition to Assets</b>	 <b><u>\$8,342</u></b>	 <b><u>827</u></b>	 <b><u>938</u></b>
 <b>Assets -- End of Year</b>	 <b><u>\$8,342</u></b>	 <b><u>\$9,169</u></b>	 <b><u>\$10,107</u></b>
 <b>New York City and MAC Securities</b>	 <b>\$ 855</b>	 <b>\$1,809</b>	 <b>\$3,309</b>
Owned at Beginning of Year			
New Purchases From Net Addition to Assets	\$ 623	\$ 827	\$ 938
New Purchases from Proceeds of Collateral Loans	<u>331</u>	<u>673</u>	<u>-0-</u>
Total Additions of Such Securities	<u>954</u>	<u>1,500</u>	<u>938</u>
 <b>New York City and MAC Securities</b>	 <b><u>\$1,809</u></b>	 <b><u>\$3,309</u></b>	 <b><u>\$4,247</u></b>
Owned at End of Year			
 <b>Ratio of Total Assets Invested in New York City and MAC Securities</b>	 <b>21.7%</b>	 <b>36.1%</b>	 <b>42.0%</b>

2.45 million continuation  
1.0 11/100

FOOTNOTES

1. Employer Contributions for the Fiscal Year 1975-76 were obtained from the Actuary's letter to the Retirement Systems.

Employer Contributions for the later Fiscal Years were estimated to increase at the rate of 10% a year. When finally calculated, they will be determined on the following bases -

<u>Contribution Year</u>	<u>Calculated on Payroll Base Of</u>
1975-76	June 30, 1974
1976-77	June 30, 1975
1977-78	June 30, 1976

It is assumed there will be no reduction in Employer Contributions on account of "excess interest".

2. Employee Contributions were assumed to remain constant at their present level.

3. Investment income was calculated on the basis of the average of the total assets during the year by using the following rates of investment income.

MAC Securities	9.0%
All Other Assets	6.0%

4. Benefits and Other Payments include all disbursements listed in the Comptroller's Report, other than those relating to the buying and selling of securities.

MEMORANDUM

February 6, 1976

To: JZ, KA, DK, VM, RW, GK  
From: RDH *Ray Houston*  
Re: Fringe and Pension Benefits

A. Present Costs

The City of New York in fiscal year 1976 will spend over \$1.8 billion on fringe and retirement benefits for its employees, as follows:

Pension Systems (actuarial and non-actuarial)	\$1300 million
Social Security	200
Union Annuity Funds	30.9
Health and Hospitalization Insurance	170
Union Welfare Funds	124
Uniform Allowances	18.9
Training Funds	0.8
Total	\$1844.6 million

*negotiable*

The attached appendices present cost data on each benefit and some discrete proposals.

B. Rationale for Action

For the following reasons, I would recommend that reductions in this area be given a very high priority by the City:

1. Potential savings are enormous;
2. Reductions here can be made without cutting services, laying off employees, and increasing unemployment and welfare costs;
3. Savings can be realized during fiscal year 1977 and need not wait on fiscal year 1978;
4. Realization of savings here is relatively easy with regard to time, staff resources, and issue complexity compared to, say, cutting similar amounts from agencies such as HHC, CUNY, or the Board of Education.

C. Scenario

1. Adoption of position by City in upcoming negotiations that it will not offer unions certain of the negotiated benefits received in the past. Among the benefits falling within this area, in whole or in part, are (a) union annuity funds, (b) health and hospitalization insurance; (c) union welfare funds; (d) uniform allowances; (e) training funds (pension and social security reductions are matters involving state and federal law).

2. Probable, indeed almost certain, rejection of City's position by unions in negotiations.

3. Arbitration of issue as soon as possible after 7/1/76 in order to soften impact of "status quo" provision which carries over existing benefits until new contract is settled either by negotiation or arbitration.

D. Discussion

1. Based on my experience in representing the City in arbitrations, I believe the City could win an arbitration on a reduction of some of these benefits.

2. The most likely candidates for elimination, reduction, or postponement are the following: (a) union welfare funds and (b) union annuity funds. No other cities provide these benefits; neither benefit is essential to employees; both benefits supplement already generous benefits, e.g., health insurance and pensions plus social security.

3. Since City employees already have given up some benefits and will, in all likelihood, receive no general pay increases during the rest of financial plan, the equity in moving further against City employees is not clearcut. However, what are the other options? Can the City realistically expect to cut enough by other means to meet the dictates of the financial plan? And looking beyond the financial plan, can the City afford to maintain fringe and pension benefit levels that are so high?

4. If this strategy is to be pursued, a number of high-level decisions have to be reached soon.

## APPENDIX ONE

## PENSIONS

City Contribution - Fiscal Year 1976 \$1,299.66

Funding (\$ in millions)

NYCERS	\$530.00
TRS	352.87
PD	175.00
FD	51.20
Bd. of Ed.	17.28
CIRS	11.00
Libraries	6.35
TIAA	17.40

Subtotal \$1,161.10

### Non-Actuarial:

PD	31.35
FD	38.26
Street Cleaning	5.40
City Supplemental	45.00
Teacher Supplemental	18.33
Miscellaneous	.22
	<u>\$ 138.56</u>

### INCREASED TAKE HOME PAY

Under the increased take home pay provision, the City and its various agencies pay a fixed percentage of the employee's contribution to the retirement system. The employee's contribution to the retirement system is reduced accordingly. These percentages are now 5 percent for teachers and uniformed employees, and 4 percent for others.

Effective April 1, 1976, the ITHP contribution rates will be halved to 2 1/2 percent and 2 percent. This reduction will save the City \$80 million annually, but only \$20 million for the remainder of this fiscal year.

The ITHP provision expires on July 1, 1976. If the State Legislature does not renew the provision and ITHP is wiped out, the City will save an additional \$80 million per year or a total of \$160 million. Since ITHP payments, like pension contributions, are made on a two year lag, the savings would not be felt by the City for two years or July 1, 1978.

## APPENDIX TWO

### SOCIAL SECURITY

Current costs are approximately \$200 million. Given scheduled rate and base increases, costs will be higher in fiscal year 1977, perhaps \$220 million, and higher still in fiscal year 1978.

While savings from withdrawal would be substantial and withdrawal would mean approximately 6% increases in income for all employees earning under \$15,300 and about \$900 for all employees over \$15,300, the following major obstacles exist:

1. Congressional action to revise the Social Security Law would be required to let us out now (waiver of the two-year notice requirement) and to get back in at a future date (under present law, reentry is prohibited). See page 1 of attachment.
2. The City would have to act as self-insurer for a percentage of the City's workforce not yet precisely ascertained (see page 2 of attachment). About 17% of the City's employees as of 7/1/74 fall into this category. Probably this percentage is considerably lower today due to layoffs.

I recommend that we continue research on the proposal, but my opinion is that eventually the proposal will prove unworkable for political if not administrative reasons.

have to self insure for 6-10 yrs now

no impact over 10 yrs

integrate w/ pensions

out for 4 yrs

Memorandum

Re Social Security Coverage of New York City Employees

1. Can New York City opt out of U.S. Social Security coverage for its employees?

Yes, subject to certain limitations. Under Section 218 of the Social Security Act, a State is authorized to enter into a voluntary agreement for Social Security coverage of state employees or employees of political subdivisions of the State (e.g., municipal employees). New York State has entered into such an agreement with respect to New York City employees.

Section 218(g)(1) of the Social Security Act provides for termination of the voluntary agreement in its entirety or with respect to any coverage group as follows:

"(g)(1) Upon giving at least two years' advance notice in writing to the Administrator, a State may terminate, effective at the end of a calendar quarter specified in the notice, its agreement with the Administrator either -

(A) in its entirety, but only if the agreement has been in effect from its effective date for not less than five years prior to the receipt of such notice; or

(B) with respect to any coverage group designated by the State, but only if the agreement has been in effect with respect to such coverage group for not less than five years prior to the receipt of such notice."

Thus, while New York City itself does not have the power to opt out of coverage, New York State could do so for City employees as a whole or for any coverage group, subject to the two years' advance notice requirement. If a shorter period of advance notice is desired, an amendment to the Social Security Act would be needed.

2. If New York City (through the State) opts out of Social Security coverage, can it later opt in?

No. Section 218(g)(3) of the Social Security Act contains a flat prohibition against renewed coverage once a voluntary agreement for coverage has been terminated. Thus, an amendment to the law would be necessary to permit renewed coverage.

3. How would employees' Social Security retirement benefits be affected if the City (through the State) elected to discontinue Social Security coverage?

Social Security benefits are based solely on an employee's record of earnings in employment covered by Social Security. Earnings up to specified maximums in each year are averaged for a specified number of years, depending upon the employee's year of birth. It is important to note that years in which no earnings accrue under Social Security will affect the employee's Average Monthly Wage - the basis of all Social Security benefits.

In order for a worker to obtain retirement benefits, he must be a "fully insured" individual. This term means that the employee must have at least one calendar quarter of coverage (whenever acquired) for each calendar year elapsing after 1950 (or, if later, the year in which he attained age 21) and before the year in which he attains age 62. A calendar quarter of coverage is one in which the worker has earned a minimum of \$50. Any individual who has acquired 40 quarters of coverage is fully insured for life and is eligible for retirement benefits regardless of the absence of further coverage. Currently, any individual with less than 24 (22 quarters for women) quarters of coverage is ineligible for retirement benefits; individuals whose quarters of coverage fall between 23 and 40 may or may not be eligible for benefits when they reach retirement age. Employees who, at the time coverage is discontinued, have not accumulated the required number of quarters will be ineligible for retirement benefits.

In order for a disabled employee to obtain disability benefits, he must satisfy two requirements:

- 1) he would have been fully insured had he attained age 62 and
- 2) he has at least 20 quarters of coverage in the most recent 40 quarter period.

It is very important to recognize that any worker who reaches age 65 and is not entitled to monthly Social Security insurance benefits is also ineligible for hospital insurance benefits under Part A of Title XVIII (Medicare).

## APPENDIX THREE

## UNION ANNUITY FUNDS

<u>Employee Group</u>	<u>Per Diem Cost</u>	<u>Approximate No. of Employees</u>	<u>Approximate FY 1976 Cost</u>
Fire Fighters	\$1.00	10,300	\$2.69 million
Fire Officers	Up to \$2.65	1,700	1.18
Patrolmen	\$1.00	23,000	6.00
Police Officers	Up to \$2.65	5,000	3.46
Housing Police Officers	\$1.00 Up to \$2.65	900 200	.23 .14
Transit Police Officers	\$1.00 Up to \$2.65	2,970 400	.78 .28
Corrections Officers	\$1.00 Up to \$2.65	3,000 300	.78 .21
Sanitation Workers	\$1.00	9,500	2.48
Officers	Up to \$2.65	1,500	1.04
Teachers <sup>1</sup>	\$400/year	NA	11.6
Supervisors	\$550/year	NA	

1. At the maximum salary step only

## UNION ANNUITY FUNDS

### Discussion

Since 1968 the City has contributed per diem amounts toward the purchase of annuities for certain employee groups. With the exception of the teachers, annuity fund payments are made directly to the employee unions which administer the funds. Payment on behalf of teachers is made directly to the Teachers Retirement System. The approval of the teacher's annuity payments by the State Legislature in 1970 might possibly give them constitutional protection. Annuity payments for other employee groups are contractual arrangements.

Retired transit workers get a lump sum payment of \$500 per year in addition to their pensions. These payments cost approximately \$5.0 million per year.

## APPENDIX FOUR

### HEALTH INSURANCE COSTS<sup>1</sup>

City Contribution - Fiscal Year 1976 \$170,000,000

Number of Contracts<sup>2</sup> 430,000  
Average Cost Per Contract \$377.00

City Contribution - Fiscal Year 1977 \$184,000,000

(Assuming new rate increases are approved  
by the Board of Estimate)

Number of Contracts 412,000  
Average Cost Per Contract \$446.00

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1. Figures include Off Track Betting, Board of Education, Board of Higher Education, Health and Hospitals Corporation, Transit Police, Cultural Institutions, and retired employees.

2. Contract count does not equal the number of active and retired employees because some employees, such as a single parent with child, count as two contracts. Therefore, the cost per employee is higher than cost per contract. On September 30, 1975, approximately 300,000 active employees and 79,000 retired employees were covered. The number of contracts, at that time, was 430,000.

OPTIONS FOR HEALTH INSURANCE COSTS REDUCTION

All options need union approval.

1. Freeze the City's contribution at fiscal year 1976 rates and pass on any increases to City employees. This action may save the City \$22 million in fiscal year 1977 if the Board of Estimate approves rate increases currently before it.
2. Offer City employees only one health insurance plan instead of three. During fiscal year 1976, at fiscal year 1976 rates, the City would have saved approximately \$13.5 million if it had offered employees only the GHI plan. Current cost of coverage varies by as much as \$78 dollars per contract depending on the insurer.
3. Have employees earning a certain salary and above pay a portion of their health insurance costs. Since the Internal Revenue Service regulations permit employees to deduct up to 50 percent of a maximum of \$300 in health insurance premiums, or \$150, the employees effective rate would be less than what the City currently is paying. Many private sector employers have various fee-splitting arrangements.
4. The City pays the full cost of health insurance for only active and retired employees, and employees pay additional cost of covering wives, husbands, and children. At current rates under the GHI plan, the cost of coverage for an individual is \$183.00; the cost for a family is \$522.00.

2  
This policy of covering all members of an employee's family cost the City nearly \$86 million in fiscal year 1976.

#### HEALTH INSURANCE - HISTORY

1947 - The City of New York agreed to pay 50 percent of the premium for Health Insurance Program (HIP) and Blue Cross Insurance for all employees who elected to be covered.

1965 - In contract negotiations with municipal unions, the City agreed to offer all employees a choice of three health insurance programs. In addition, the City agreed to raise its contribution to 75 percent immediately and to 100 percent within a year.

1966 - Health insurance coverage was extended to all retired City employees retroactively.

**HEALTH INSURANCE RATE**  
**FISCAL YEAR 1976**

<u>Type Contract</u>	<u>Cost Per Contract</u>
<b><u>Health Insurance Plan (HIP)</u></b>	
Individual	\$196.36
Parent and Child	392.72
Husband and Wife	488.24
Family	598.32
Senior Care	64.34
<b><u>General Health Insurance (GHI)</u></b>	
Individual	183.36
Parent and Child	366.84
Husband and Wife	446.52
Family	522.24
Senior Care	71.52
<b><u>Major Medical (GHI - Type E)</u></b>	
Individual	219.72
Parent and Child	444.44
Husband and Wife	515.40
Family	597.24
Senior Care	74.40

## APPENDIX FIVE

### WELFARE FUNDS

<u>City Contribution - Fiscal Year 1976</u>		\$124,000,000
Uniformed Employees	59,000 @ \$400	\$23,600,000
Teachers and Supervisors		
Board of Education	65,000 @ \$370	24,050,000
Faculty		
Board of Higher Education	13,000 @ \$340	4,400,000
Other City Employees	120,000 @ \$350	42,000,000
Part-Time Employees	10,000 @ \$200	2,000,000
Retirees	80,000 @ \$350	28,000,000

OPTIONS FOR WELFARE FUND COST REDUCTION

All options need union approval.

1. Reduce the welfare fund benefit by \$50 per employee. This action would save the City \$17.3 million in fiscal year 1977.
2. Eliminate welfare benefits for retirees who already receive pensions, social security benefits, medicare (65 years or older), plus the City's basic health insurance program. This reduction in coverage would save the City \$28 million.
3. The City itself manage the welfare funds and provide the benefits. The City may be able to provide the same basic supplementary benefits at a reduced cost. Moreover, administrative savings would be achieved and there would be less strain on the City's cash flow position.
4. Eliminate welfare funds completely since the benefits provided by these funds are not generally benefits provided completely free of charge by any other employers. Instead, the City could offer employees dental insurance, optical insurance, and life insurance programs for which the employees would pay the premiums.

## WELFARE FUNDS

### Discussion

The City pays welfare fund contributions directly to municipal unions who then administer the funds. These monies are used to purchase benefits that supplement the basic health insurance program such as extended hospital care, dental care, eyeglasses, drug prescriptions, counseling, and some legal services.

The City first began to provide welfare funds in 1965. In the last City-Wide contract, signed May 6, 1974, covering the period July 1, 1973 to June 30, 1976, the City agreed to provide partial welfare funds for part-time, hourly, per diem, per session, and seasonal employees who work at least one-half the regular hours of a full time employee. Moreover, the City agreed to provide full welfare fund benefits as of January 1, 1974 to all employees who retired after June 30, 1970. Similar provisions are contained in contracts not covered by the City-Wide.

In early 1975, thirteen municipal unions agreed to a reduction in the welfare fund contribution totaling slightly more than \$8 million. (See attached sheet) The reduced payments were scheduled to be made over an eighteen month period from February 1, 1975 to June 30, 1976.

WELFARE FUNDS  
SUPPLEMENTAL AGREEMENT (1975)

<u>Union</u>	<u>Amount of Reduction</u>
District Council 37	\$5,500,000
Social Service Employees Union	1,000,000
Uniformed Sanitationmen's Association	1,000,000
International Brotherhood of Teamsters - Local 237	306,000
Service Employees International Union - Local 144	102,000
Pavers and Roadbuilders	42,500
Communication Workers of America - Local 1180	39,333
Communication Workers of America - Local 1182	20,000
Communication Workers of America - Local 1181	3,500
Communication Workers of America - Local 1183	8,500
Municipal Guild of Radio and Television Technicians	8,500
Civil Service Bar Association	8,500
Licensed Practical Nurses	8,500.
TOTAL	<u>\$8,047,333</u>

## APPENDIX SIX

### UNIFORM ALLOWANCE

City Contribution - Fiscal Year 1976      \$18,900,000

Approximate number of City titles  
receiving uniform allowance      190

Examples:

<u>Title</u>	<u>Allowance</u>
Patrolman	\$265
Fireman	265
Public Health Nurse	200
Marine Engineer	200
Aqueduct Captain	170
Speech & Hearing Therapist	120
Nurse's Aide	110
Ambulance Technician	110
Food Service Supervisor	90
Swimming Pool Operator	65
Bridge Operator	65
Deckhand	65
Water Plant Operator	45

OPTIONS FOR UNIFORM ALLOWANCE COST REDUCTION

All options require union approval.

1. Eliminate allowances completely. Almost all employees in the private sector, and most public sector employees, provide their own clothing. Moreover, some City employees who, in fact, receive a uniform allowance do not have a job that requires them to wear a uniform.
2. The City contracts with uniform suppliers and provides uniforms, as they are needed, directly to employees who actually wear them.
3. Reduce uniform allowances and restrict to employees who are required to wear them.

## APPENDIX SEVEN

### TRAINING FUNDS

#### PAID DIRECTLY TO UNIONS

<u>Total City Contribution - Fiscal Year 1976</u>	\$755,000
District Council 37	\$690,000
Communication Workers of America Local 1180	65,000

#### OPTION

This option requires union approval.

Eliminate these funds completely. Training employees is a management, not a union, function.

Re: NY 1/13/76

STATE OF NEW YORK  
EXECUTIVE DEPARTMENT  
DIVISION OF THE BUDGET  
ALBANY

**MEMORANDUM**

**To:** Peter Goldmark  
**From:** Bentti O. Hoiska  
**Subject:** New York City Police Pension

**Date:** January 13, 1976

The New York City financial crisis has generated considerable interest in cost cutting. The reduction of City pension costs has received particular attention and is the subject of the attached report. The report estimates the cost reductions which would result if the service requirement for retirement for City police were increased from 20 to 25 years. Having these estimates will help policymakers to judge whether such a plan change is worth the political price required to make the change.

Attachment

CC: H. Elish  
J. Schrauf

## INCREASING THE SERVICE REQUIREMENT FOR NEW YORK CITY POLICE RETIREMENTS

### I. Introduction

In this report we estimate the pension cost reductions which would result from increasing the service requirement for retirement for New York City policemen. We show that changing from a 20-year plan to a 25-year plan, each with a 2.5 percent increased-take-home-pay (ITHP) provision, would result in a first-year saving of \$1.8 million (or 1.4 percent) and an ultimate annual saving of \$37.5 million (or 30.2 percent). Since other uniformed City employees have pension benefits comparable to those of the police, similar (percentage) savings could be realized if their service requirement were also increased.

### II. Contribution Rates

The table below contains employee and employer contribution rates for 20, 25, and 30-year service retirement plans with 0, 2.5, and 5 percent ITHP provisions. As indicated, the employer contribution rates are quite sensitive to plan changes. They vary from a high of 25.5 percent for a 20-year plan with a 5 percent ITHP provision to a low of 8.4 percent for 30-year plan with no ITHP provision.

These rates are computed for a single hypothetical policeman entering the force at age 25 and retiring as soon as he becomes eligible to do so. Aside from the assumption that retirement occurs at the earliest possible date, the computations are based upon the actuarial assumptions adopted by the Police Pension Fund. The computed contribution rates completely fund the employee's service pension (including vesting) and the withdrawal,

disability and death benefits tied to his contributions and the ITHP contributions made on his behalf. The bulk of the cost of disability pensions and death benefits has been ignored because we are not considering changes in these benefits.

Contribution Rates for New York City  
Police Service Pensions  
Entry Age 25

<u>Service Requirement (Years)</u>	<u>ITHP Rate (Percent)</u>	<u>Employee Rate (Percent)</u>	<u>Employer Rate (Percent)</u>
20	0.0	6.1	21.6
20	2.5	3.6	23.5
20	5.0	1.1	25.5
25	0.0	3.8	13.6
25	2.5	1.3	15.4
25	5.0	0.0	16.3
30	0.0	2.3	8.4
30	2.5	0.0	9.9
30	5.0	0.0	9.9

III. Pension Cost Reductions

Since the State Constitution prohibits an employee's pension benefits from being diminished after he becomes a member of a public retirement system, such benefits can only be diminished for new members. Accordingly, cost reductions arising from plan changes are initially small, gradually increase as new-plan members replace old-plan members, and attain a maximum when all old-plan members have been replaced.

Thus, we must project cost reduction figures several years into the future to characterize adequately an increase in service requirements.

A ready alternative to the current 20-year plan is a 25-year plan. To determine the cost reduction resulting from the adoption of a 25-year plan, we assume that the ITHP rate is 2.5 percent and that the size of the police force remains constant (i.e., attrition equals replacement). We also use the following data:

Average annual salary for policemen aged 25 (June 30, 1973)	=	\$13,800
Average annual salary for all policemen (June 30, 1973)	=	15,400
Gross attrition rate for policemen (1973-74)	=	5.3%
Size of police force	=	30,000
Normal attrition [= .053(30,000)]	=	1,600
City contribution rate for 20-year plan minus rate for 25-year plan, each with 2.5 percent ITHP (=23.5-15.4)	=	8.1%

The cost reduction in the first year following the plan change is \$1.8 million [= .081(1,600)(13,800)]. This figure is the product of the difference between the City contribution rates for the two plans, new-plan members (i.e., attrition for one year), and the annual salary for a new entrant aged 25. The reduction in the second year would be about twice as large, that is \$3.6 million. After approximately 20 years all 30,000 old-plan policemen would have been replaced so that from then on the annual savings would become \$37.5 million [= .081(30,000)(15,400)].

To put these figures in perspective, we note that the \$1.8 million first-year saving equals 1.4 percent of the 1974-75 contribution of \$134.4 million [divided by  $(1.04)^2$  to eliminate interest for two years due to lagged payment of the 1972-73 contribution] to the Police Pension Fund and the \$37.5 million ultimate annual saving equals 30.2 percent of that contribution. Furthermore, in terms of June 30, 1973 salary levels and a 30,000 member force, the recent decrease in the ITHP rate from 5.0 to 2.5 percent will save the City roughly \$9.2 million [ $= .02(15,400)(30,000)$ ], while changing from a 20 to a 25-year plan would save the City \$9 million [ $= 5(1.8 \text{ million})$ ] in the fifth year. The saving would be less than \$9.2 million during the first four years and greater during the sixth and subsequent years.

#### IV. Some Technical Notes

The following points should be considered when interpreting the above results:

1. To keep our figures comparable over time, June 30, 1973 salary levels have been used throughout. Had we recognized that salary levels increase over time, then our year-by-year cost reduction figures would have risen more rapidly. To transform our results to a current dollar basis, we would have multiplied the figures in Section III by an index measuring salary levels increases occurring since June 30, 1973.
2. If a 25-year plan were adopted now, the first-year cost reduction most likely would exceed \$1.8 million because attrition is currently well above the normal level.

3. The calculated contribution rates are understated because the actuarial tables used by the Police Pension Fund are obsolete. However, since the rates for the 20 and 25-year plans are understated to about the same degree, the understatements cancel when the rates are differenced.
4. Shifting to a 25-year plan requires providing five additional years of death benefit and disability benefit coverage. Since these coverages have been largely ignored, their increased cost does not manifest itself in 25-year plan contribution rates. Although these rates are understated, the error is small and does not distort the results.
5. The employer contribution rates computed by the City Actuary exceed ours because his rates fund disability and death benefits and amortize actuarial losses, while ours do not.
6. The 2.5 percent decrease in the ITHP rate is equivalent to a true decrease of 2 ( $= 25.5 - 23.5$ ) percent in the City contribution rate. This occurs because an employee does not receive benefits from the ITHP reserve accumulated on his behalf if he withdraws before completing 15 years of service. (If he withdraws with between 15 and 20 years of service, his ITHP reserve is used to cover a portion of the cost of his vested pension.)

7. It should be recalled that City pension contributions are made with a two-year lag. Thus, for example, a cost reduction accruing during the first year after a plan change will not manifest itself in the City's cash outflow until the third year. The figures in Section III were developed on a accrual basis; they can be converted to a cash basis by lagging them two years and then adding interest for two years.

MEMORANDUM OF RECORD

Re New York City Retirement Systems

The second meeting of the Task Force on NYC Retirement Systems took place on October 14, 1975 at the Metropolitan Life Insurance Company. Those attending were as follows:

Hy Bartimer - Metropolitan Life  
Gordon Binns - General Motors  
Jim Gardiner - New York State Insurance Department  
Jonathan Schwartz - New York City Retirement Systems  
Bill Thomas - Metropolitan Life  
Bob Tilove - Martin E. Segal & Co.  
Jim Tobin - Union Carbide  
Leo Walsh - Equitable Life

Three sets of material were distributed to each member at the opening of the meeting:

- 1) Tables of actuarial assumptions deemed appropriate by the New York City Actuary for the cost calculations. He recommended basically four changes in the current assumptions -- valuation interest rate increased from 4% to 5 1/2%, a uniform but much steeper salary scale, the 1951 Group Annuity Table for mortality of disabled pensioners and the 1971 GAM table for mortality of active members and service pensioners.
- 2) Memorandum on the status of the conversion of the New York City Retirement Systems data from punch cards to electronic tape. Target date is the week of October 27.
- 3) Average annual salary increases during the past ten years for selected male and female employees of the New York City Retirement Systems prepared by the New York State Insurance Department Actuary.

Bill Thomas mentioned that letters were forwarded to the Board of Trustees of the Teachers Retirement System and the New York City Employees' Retirement System requesting that the basic tape files be made available to the Task Force as soon as possible for cost analysis. There was then a brief discussion as to the time frame for completion of all cost estimates in view of the heavy volume of decrement factors and benefit calculations required for all retirement systems. Every effort will be made to complete this project before year-end.

There were a number of different viewpoints as to appropriate mortality assumptions. Although Jonathan Schwartz recommended a standard mortality table for all active members and service pensioners for convenience in performing the calculations, he believed there were actually three levels of mortality -- (1) teachers, (2) policemen, firemen and sanitation men, (3) all others. Bob Tilove preferred to use mortality rates developed from actual experience data. He therefore recommended a review of the most recent studies on actual to expected mortality. The New York City Actuary, however, stated that such data had rather limited value since the deaths were based on dates processed rather than incurred. There could be time lags of several years. He will look into this matter and determine, if possible, the degree of distortion caused by this time lag factor. Bill Thomas inquired as to the mortality bases for the state retirement plans. The New York City Actuary felt that these rates, based on recent mortality statistics, were quite appropriate for the New York City systems. He will compare these mortality tables with the 1971 GAM table he proposed as well as actual to expected ratios assuming these bases as standards.

Bill Thomas then directed the discussion to valuation interest rates and salary scale assumptions. We were informed by the New York City Actuary that the Policemen and Firemen Funds were earning currently about 5% per annum, the New York City Employees' Retirement System 5 1/2% and the Teachers' Retirement and Board of Education Retirement Systems 6%. The main reason for the difference was the degree of equity participation -- 35% for the Policemen and Firemen Funds, 20% for the New York City Employees' Retirement System and 0% for the Teacher Retirement and Board of Education Retirement Systems. For the latter systems pension funds are invested in fixed interest securities only. Employee monies, however, may be invested in variable annuities. Bases for the asset valuation are amortized book value for bonds and cost for stocks. The latter basis might have to be modified to conform with ERISA standard which requires an adjusted market value concept. In view of the above experience, the New York City Actuary felt he could feel comfortable with a change in the current valuation interest rate from 4% to 5 1/2%. Bill Thomas suggested that consideration might be given to moving up to 6% in view of current market conditions. Bob Tilove mentioned the difficulty in getting the state legislature to approve interest rates above 4 1/2% for the state retirement plans. One state plan currently assumes 4 1/2% throughout and the other two assume 5 1/2% for the first ten years and 4 1/2% thereafter.

As for salary scale assumptions the New York City Actuary recommended a uniform scale for all plans that show annual increments of 6% to 7% at the early ages decreasing gradually to a flat 3% for ages 55 and over. Bob Tilove suggested a progressive scale derived from a snapshot approach for the most recent calendar year and adding a uniform increment of 3% or so to reflect future experience. Jim Gardiner will develop his average annual salary statistics for the Teachers' Retirement and New York City Employees' Retirement Systems by age for a number of calendar years. These two approaches may result in some modifications of the salary scale recommended by Jonathan Schwartz. It was noted that this scale was somewhat steeper than the one used in the state retirement systems.

A committee of four (Binns, Gardiner, Tilove and Tobin) was assigned to review investment performance and salary history with the New York City Actuary and determine the appropriateness and modification, if necessary, of the recommended valuation interest rate and salary scale increments. Leo Walsh will look into the mortality bases of other state and municipal retirement systems.

A number of plans assume that the employee contributions for the first twenty years accumulated at 4% interest will provide 12 1/2% of final pay. Hence the valuation assumes that the City provides for 37 1/2% of final pay for the first twenty years of service i.e. 50% -12 1/2%. Hy Bartimer suggested that in view of the recommended changes in the actuarial assumptions, it is likely that the fixed employee contribution rate will now provide less than 12 1/2% of final pay. Hence our estimates should assume that the City's share will rise above the 37 1/2% figure - possibly 40% to 42% of final pay for the first twenty years of service. The New York City Actuary will look into this matter and see if some adjustment is called for. One suggestion that we determine the actual City percentage in each individual case would not only complicate the service benefit calculation but greatly complicate the calculation of other benefits as well.

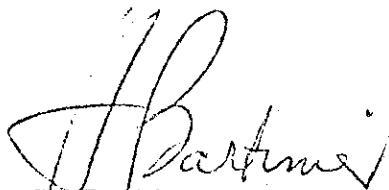
The following additional points were discussed:

- 1) Why do employees receive only 4% interest when the system is actually earning more? The New York City Actuary pointed out that the archaic mortality table partially offsets the lower interest when the accumulation is converted into an annuity.
- 2) A women's group is suing the City because of the differential mortality used for the sexes.
- 3) Due to faulty mortality data (death based on date processed rather than incurred -- as mentioned before) the New York City Actuary has developed statistics that show only a one or two year differential in the expectation of life for females vs males at the upper ages. The state retirement systems show a five to six year differential. This explains Schwartz's aversion to the use of actual to expected mortality data developed by his office.
- 4) The current funding method is the aggregate cost with frozen initial liability amortized over thirty-five years. This, in effect, funds an increasing proportion of the total liability over the future service lifetime of the current active member group. It was recommended that we also prepare estimates under the entry age normal cost method with thirty or forty year funding of the past service liability. The advantage of the aggregate method is that as new entrants replace older employees the percent of payroll tends to decrease if the experience follows the assumptions. However, if the experience losses are modest, the result may still be a relatively level percent of payroll. The entry age normal cost method allows for more flexibility and stability in contributions by varying the period of amortization of the past service

liability. Furthermore, it is by far the more popular method. The New York City Actuary noted that the current assumptions deviate so much from the experience, that his percent of payroll estimates keep rising year after year under the aggregate cost method.

- 5) Jim Tobin would like to compare typical industry pension benefits with benefits under the various New York City retirement plans. The New York City Actuary indicated that he may be able to supply typical comparable illustrations or develop suitable hypothetical cases.

The meeting broke up at 5:00 p.m. and the next one was scheduled for Tuesday, October 28, at the Metropolitan Life Insurance Company.



H. Bartimer  
Actuary

October 15, 1975

CC: All Task Force Members

## REPORT

## PUBLIC PENSION TASK FORCE

PENNSYLVANIA  
Task Force

## Concerning Public Employee Pensions in 1976

To the Board of Directors  
New York Chamber of Commerce & Industry

October 14, 1975

Gentlemen:

The spotlight of public attention centered on public employee pensions in New York State back in 1971. That was the occasion of a strike of bridge tenders and sewage disposal workers in New York City, stemming from a refusal by the State Legislature to approve a previously bargained enrichment of pension benefits for City employees.

While the City of New York was permitted under the law to bargain on pension benefits, along with a host of other subjects, all of the pension programs covering public employees must be legislated in Albany. The refusal of the State Legislature to act in this instance was the result of a sudden realization that the constant bargaining and "leap-frogging" of pension demands posed a serious threat to the economic strength of the State and its subdivisions. It was evident that liberalization of Transit Authority pensions in New York City in 1968 had stripped that agency of many key employees. Pension costs were accelerating. There were evident abuses in the application of overtime pay to swell retirement benefits, permitting retirement in some instances with pensions that exceeded the employee's base pay.

The city employees who went on strike had already been the beneficiaries of a substantially liberalized pension revision in 1968. Teachers in New York City had made enormous gains in 1970. Police and Fire employees were demanding better pensions -- retirement at half-pay after fifteen years of service, and full pay after 25 years. It was apparent to the Legislature that somewhere, this pension treadmill had to come to an end.

The 1971 strike set off a number of reactions. The Legislature enacted a law to create the Permanent Commission on Public Employee Pension and Retirement Systems, which was finally appointed in November, 1971.

The Commission had two broad assignments -- to review and report to the Legislature and the Governor on all legislative proposals dealing with public employee pensions and retirement, and to examine existing pension systems and make recommendations on them.

Chapter 503 of the Laws of 1971 attempted to place a limit on the amount of overtime or other special compensation to be included in computing the salary base for pensions, limiting the amount to no more than 20 percent greater than the pay for the prior year. While this was designed to prevent abuse of overtime, it has been successfully challenged

in the Courts by city employees as being unconstitutional, in that it reduced or impaired benefits guaranteed by the Constitution. 1/

Early in 1973 the Permanent Commission presented recommendations to the Legislature calling for sweeping reforms in public employee retirement programs in New York State. Their proposals would have increased the number of years of service required to get full retirement benefits, would have limited total retirement benefits to the employee's approximate take-home pay at the time of retirement, and would have included in the computation the social security benefit received by the employee. This new program would have applied to all future employees; existing employees would have retained the benefits of their existing systems.

After lengthy and often-times bitter public hearings, the Legislature refused to act on the Commission proposal, but did appoint a "Select Committee on Pensions" to give consideration during the summer of 1973 to the need for pension reform. In the meantime the State Civil Service Employees Association agreed to a compromise pension plan for future employees in its bargaining with the State.

Out of this process there finally evolved a proposal for pension reform, which was adopted by the Legislature. Again, this applies only to persons who became public employees after July 1, 1973. A major change, was to base an employee's pension on the average of the last three years' pay instead of on the last year of pay or on the rate of pay at the time of retirement. For some employees, the provision for retirement at age 50, or age 55 has been replaced with an age 62 retirement. Earlier retirement is still permitted, but with a reduction in the retirement benefit. There are also provisions which limit the total pension to 60 percent of the first \$12,000 of income, and 50 percent of the balance, after 25 years of service. As a result of this legislation, the cost of financing public employee pensions will be somewhat reduced.

However, the failure of the Legislature to provide for integration of pensions with social security system benefits, which are also payable to city and state employees, may see those planned savings balanced off by higher Federal Social Security taxes paid by the cities and state. These taxes, which now exceed the total payments into New York City's five actuarial pension systems a decade ago (in 1964-65 the five actuarial systems received contributions of \$236.3 million; 1974-75 social security costs are estimated at \$241 million) could easily absorb any savings accounted for by the new system. Virtually all of the recent analyses of the Federal Social Security system and its financing suggest substantially higher taxes will be required to support the system in the years ahead.

The 1973 Legislature also enacted into law a prohibition against further collective bargaining relative to pension benefits, and called for a new concept of coalition bargaining to be developed.

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1. The State Constitution declares that public employee pensions are a contractual right that cannot be diminished or impaired. This provision has, over the years effectively barred any reduction in benefits for existing employees. Numerous statutes which provide for one-year changes, designed to prevent them from being frozen into pension systems, have been adopted.

Both the pension reform act of 1973 and the an on collective bargaining were enacted with expiration dates. The crucial year is 1976. Unless the Legislature acts to extend or modify these laws, they will expire on April 1, 1976.

Thus it can readily be predicted that 1976 will see a new period of discussion, argument and pressure on the general subject of public employee pensions in New York State. The lines will be drawn between the public employee organizations, which would undoubtedly prefer to see the 1973 legislation die a quiet death from inaction, and those organizations and individuals concerned with rising public costs, who would like to have seen permanent and more stringent legislation adopted in 1973. Inaction by the Legislature would presumably result in a blanketing of employees hired since 1973 into the older, existing and more liberal pension systems. This would increase future retirement costs.

#### LOOKING AHEAD ON PENSION PROBLEMS

In March of 1975 the Permanent Commission released a report entitled Financing the Public Pension Systems, Part I: Actuarial Assumptions and Funding Policies. A second report, dealing with investment policies of the pension systems is reportedly under way by the Commission.

The March Report deals with the actuarial funding of the major pension systems -- three State and five City pension systems. It points out that these programs are required by law to be "actuarially funded", so that the yearly payments to the systems are approximately equal to the cost of the benefits earned during the year by employees. Failure to provide sound actuarial funding leads to inadequate funds to meet pension obligations and ultimately to substantially larger payments for pensions out of then current operating revenues in future years when employees are retired.

This Report found that, while the State has updated its actuarial assumptions, New York City has failed to do so. It states that "As a result, the New York City systems' actuarial assumptions continue to be out of touch with reality" (p. 12 of Report). It goes on to report that

"Amazingly, the assumptions used for the New York City Employees' Retirement System were prepared for a 1914-1918 Commission on Pensions from the City's records of experience from 1908-14-- more than a half-century ago. Data from the same period is used for the City Teachers' system. The Police and Fire systems, created in 1940, use data based upon the same 1908-14 experience, with only slight modification. With the exception of some changes made in the 1940's with respect to mortality after retirement and interest credits, no changes have been made in the assumptions since these systems were first established." (p. 13)

Since the amount of funds provided annually to build the reserves required for retirement are based on outmoded actuarial data, the net effect is to under-estimate the amount required, and to under-fund the systems.

For example, the Report points out that the City systems substantially under-estimate life expectancy of employees;

- far under-estimate police and fire service-related disabilities;
- understate seriously the rate of pay increase -- which has serious cost implications because City pensions are based on pay at the time of retirement, or the last year's pay.

The Report makes the following comments relative to the New York City pension systems:

"The City's refusal to adopt realistic actuarial assumptions has resulted in a systematic failure to pay current pension costs, thereby increasing future liabilities and, hence, the retirement contributions in future years." (p. 30)

"The City's refusal to adopt realistic actuarial assumptions has led to the approval of benefit increases without full realization of the additional costs involved, resulting in a further increase in the annual contribution rate." (p. 31)

"Despite the fact that the estimates of current costs are unrealistically low, the City has failed to pay even those official costs - thereby leading to a further spiraling in the annual contribution rate." (p. 32)

The impact of underfunding is found in the Report's Table 10, which shows the available reserves in the City Pension Systems. Between 1967 and 1973 the Reserves for Active Members -- the funds available to cover the benefits earned by currently employed members -- dropped from \$2 billion to \$1.522 billion. The impact of this drop is better understood when one realizes this was a period of rapid increase in pay as well as in pension fund membership.

Pension fund data for 1967 and 1973 indicate that membership increased from 255,967 to 331,425 or 29.5 percent. Covered payrolls rose from \$2.106 billion to \$4.089 billion, or 94.1 percent. And during this same period, the City of New York adopted a series of pension changes which vastly increased the City's liabilities through liberalization of benefits to all employees. Clearly, this was not a period in which the reserves for active members should have been permitted to drop by 25 percent!

#### COMMISSION RECOMMENDATIONS

The Permanent Commission's Report recommends that Retirement and Social Security Law be amended to require the City actuary to prepare and submit "appropriate recommendations" with respect to each actuarial assumption at least quinquennially and that the Superintendent of Insurance be required to review and approve or disapprove such assumptions. Further, upon approval by the Superintendent of Insurance and recommendation of the actuary or Superintendent, the head of each pension system should be required to act on those assumptions within sixty days. Failure to act, or submission of a report stating reasons for not acting, by the head of the pension system, could result in intervention by the Superintendent of Insurance to force adoption of the assumptions.

A proposal was also made to establish an actuarial advisory committee to assist the Superintendent.

Finally, the report noted that adoption of adequate actuarial standards

would undoubtedly increase New York City contribution levels, and suggested that this might require other funding alternatives "on a one-time exception basis."

CHAMBER OF COMMERCE AND INDUSTRY  
RECOMMENDATIONS

The special Ad Hoc Pension Committee recommends that the following position be approved:

1. That the Chamber of Commerce and Industry of New York City is firmly of the belief that there must ultimately be further reforms in public employee pensions. Current forecasts of costs for New York City, based on current, obviously inadequate actuarial assumptions in use by the City, suggest that total retirement costs, including social security taxes, will exceed \$2 billion by 1980.

We do not believe that efforts to reform the public employee retirement programs can be properly approached until such time as the costs of existing systems are fully apparent to the persons most concerned with them -- and this includes public officials, public employee unions and their members, the State Legislature and the general public.

The first step in this process must be to obtain a true measure of the liabilities facing the City and State of New York -- and particularly the City -- by ascertaining the impact of utilizing up-to-date actuarial assumptions in computing future contributions to the pension and retirement programs. Accordingly, we endorse the Commission recommendations. We would argue further that any analysis of costs of pensions and retirement programs must include the cost of other retirement commitments, including social security and supplemental pension benefits currently in use to help older pensioners meet increasing costs due to inflation.

2. We urge that the Legislature make no effort to reform or modify temporary legislation currently in effect but rather, that such legislation be extended for three years, pending full and complete review of actuarial assumptions and determination of their impact on future City and State finances.

We urge extension of the ban on the collective bargaining of pension benefits, which we consider essential until all of the facts are known.

It must be noted that these pension liabilities, the dimensions of which are obviously unclear, constitute a contractual commitment by New York City. To the extent that they are under-funded, they represent a form of debt which must be amortized over the years ahead. Until such time as we have a reliable measure of those liabilities, every effort must be made to prevent their magnification by increasing benefits.

3. We urge the integration of public employee pensions with Social Security.

At the time municipal employees were brought under the Social Security system in 1957 both the tax per employee and the benefits payable were relatively modest. From a tax of 2% on \$4200 (\$84) the employer share has grown to 5.85% on \$14,100 (\$825).

Benefits have increased so that they represent for many a primary source of retirement income. The Permanent Commission on pensions (Kinzel) recommended some integration of the retirement systems with Social Security, as had the City's own consultant in 1962 (Martin Segal and Co.). With all forecasts indicating increasing costs in the future as benefits, tied to inflation, are increased, integration of the two systems becomes essential to keep total retirement costs within manageable fiscal limits.

4. We urge the discontinuation of uniformed forces Annuity Fund payments. Members of the Police, Fire, Sanitation, Corrections, Housing Police and Transit Police are all beneficiaries of a "union annuity fund" plan inaugurated through collective bargaining in the late 1960's. Payments to the unions are made by the City at the rate of \$1 a day for each day worked (with larger payments for superior officers). These funds are invested by the unions, and may be withdrawn at the time of retirement as an additional retirement benefit. They cost New York City about \$17-\$18 million a year. Declared illegal by the State Comptroller in a special audit report (1972) on the basis that they had not been legislated and were thus in conflict with pension system laws, these payments continue to be made. The City argues that this is a form of deferred compensation. The Permanent Commission recommended that these payments be prohibited by law. A similar plan is provided for teachers who have reached maximum (\$400 a year) but this has been legislated. Efforts should be made to stop these questionable payments to the unions, and recover the funds already paid out.

5. Finally, we urge that agreements which include frozen pay increases in the computation of pension benefits be legislated out of existence.

In winning agreement to the current "pay freeze" there are indications that the City has agreed that, even though the increases in pay have not been made, the employee's pension benefits will be tied to the total current earnings plus the amount that would have been paid. This is another "pension sweetener" which will add substantially to pension costs. It adds another element of benefits which must ultimately be funded, in pension systems which are, it is widely agreed, already underfunded. It opens the way for future abuses, in which any major group of employees might be encouraged to retire by granting them a major "phantom" pay increase, which, in one year, would materially increase their retirement benefits. Since pensions are now based on the pay at the time of retirement (uniformed forces) or the last year of pay, this device has serious financial implications for the City. Legislation is imperative to prohibit the carrying out of these policies.

Respectfully submitted,

Richard Farrell  
Chairman

Note: See reverse side of this sheet for Committee List.

\*\*\* PUBLIC PENSION TASK FORCE \*\*\*

CHAIRMAN

Richard Farrell  
GAF Corporation

Clemens G. Arlinghaus  
Metropolitan Life Insurance Company

Irving Matloff  
Bulova Watch Company, Incorporated

Albert X. Bader, Jr.  
Simpson, Thacher & Bartlett

Charles A. Moran  
Manufacturers Hanover Trust Company

Paul L. Bradley  
EBASCO Services, Incorporated

Aaron S. Sadove  
Consolidated Edison Company

Thomas F. Delaney  
Metropolitan Life Insurance Company

Douglas Soutar  
ASARCO Incorporated

Roland Delfausse  
Economic Development Council

Arthur A. Windecker  
Equitable Life Assurance Society  
of the U. S.

William P. Witman  
New York Telephone Company

\*\*\*\*\*  
New York Chamber of Commerce & Industry  
Staff Representative  
\*\*\*\*\*

\*\*\*\*\*

230 West 41 Street, New York, N.Y. 10036 594-2600

PER/AL/MS

**Jack Bigel** president

MEMORANDUM

September 2, 1975

To: Jack Bigel  
From: Tony Gajda  
Subject: Estimates Of Numbers Of City  
Employees Who Are Eligible  
For Retirement; Estimated  
Payroll Savings; And,  
Estimated Additional Pension  
Appropriation Required.

As you requested, an analysis of the number of City employees who are eligible for retirement has been performed. All data used in this analysis is taken as of June 30, 1974, as recorded in the Office of the Actuary of the five actuarially-reserved retirement systems. No data is yet available for June 30, 1975 because of personnel losses within the Office of the Actuary and also because of the relatively unsettled situation in various City agencies with respect to workforces, lay-offs, etc.

Number of Employees Eligible for Retirement

Table 1 shows the number of City employees, including those of the Boards of Education and Higher Education, Health & Hospitals Corp., etc. who satisfy the eligibility requirements for service retirement.

The total number of employees eligible for retirement, 62,927, is derived by using minimum requirements for eligibility. The impact of this method can best be seen in the C.P.P.-I.S.F. plans of the New York City Employees Retirement System. The C.P.P.-I.S.F. Plans, which covers all non-uniformed employees, permits retirement at or after the attainment of age 55. If an employer attains age 55 and renders 25 years of service, he will receive a retirement allowance equal to 55% of his final year salary. Although only 7,948 employees have rendered 25 or more years of service, 37,728 employees are age 55 or older and are, therefore, eligible for retirement.

Table 1: Number of City Employees Eligible For Retirement

Retirement System	Eligibility Requirements For Service Retirements	Number Eligible As of June 30, 1974	
1) Police	20 Years of Service Regardless of Age	4,698	(a)
2) Fire	20 Years of Service Regardless of Age	2,671	(b)
3) Teachers	20 Years of Service, Payable @ Age 55; or Age 55 Regardless of Service	13,132 (20+) 12,796 (55+)	(c) (d)
4) NYCERS			
. CPP-ISF	25 Years of Service and Age 55; or Age 55 Regardless of Service	7,948 (25+) 37,728 (55+)	(e) (f)
. Sanitation	20 Years of Service, Regardless of Age	3,256	(g)
. Police (Ancillary)	20 Years Service, Regardless of Age	778	(h)
5. Board of Education	Same requirements as CPP (NYCERS)	1,000	(i)
Total Eligible = (a)+(b)+(d)+(f)+(h)+(i)+(j)		62,927*	

\*Does not include 8,340 members of the Transit 20-Year Plan who were eligible to retire on June 30, 1974.

This method of using the minimum eligibility requirements is employed only in C.P.P.-I.S.F. plans and the Teachers' pension system.

Finally, the 62,927 employees who are eligible for service retirement excludes other types of separation from service, such as disability retirement, deaths, and termination.

Past experience has indicated that approximately 2,000 disabilities and 2,200 deaths can be expected throughout the five systems. Current conditions in the City of New York make it impossible to predict the number of terminations.

Salaries of Employees Eligible for Retirement

Table 2 combines the number of employees who are eligible for retirement along with the estimated salaries of each of the general categories of employment.

Table 3 shows that the 62,927 employees represent a payroll cost of approximately \$1,070,406,000, or slightly less than 10% of the New York City budget.

Table 3 shows that if, in addition to the normal number of retirements, another 14% of the eligibles retire, the payroll savings to the City will be approximately \$163,141,000. For purposes of this estimate, it has been assumed that the additional retirements will occur in the same proportion as the numbers eligible in each of the retirement systems.

Table 4 shows the payroll savings to the City that can be generated by various levels of retirement in excess of the normal rate.

Table 2 : Salaries of City Employees Eligible  
for Retirement

<u>System</u>	<u>Number</u>	<u>Average Salary</u>	<u>Total Payroll</u> (000)
Police	4,698	\$20,000	\$93,960
Fire	2,671	20,000	53,420
Teachers	12,796	21,000	268,716
NYCERS			
• CPP	37,728	15,000	565,920
• Sanitation	3,256	18,000	58,608
• Police (Ancillary)	778	19,000	14,782
Board of Education	1,000	15,000	15,000
TOTAL			\$1,070,406

Table 3 : Estimated Payroll Savings Resulting From Increased Rates in Retirement

Number of Retirements  
In Excess of the Normal  
Rate:\*

		<u>Payroll Savings (000)</u>
- N.Y.C.E.R.S.		
CPP-ISF	5,281	\$ 79,215
Transit-20 Year	1,167	21,006
Police Forces	<u>109</u>	<u>2,071</u>
TOTAL	7,013	\$102,292
- N.Y.C.T.R.S.	1,815	\$ 38,115
- Police	658	13,154
- Fire	374	7,480
Board of Education	<u>140</u>	<u>2,100</u>
TOTAL	9,544	\$163,141

\*It is assumed that 14% of eligibles will be retired. The proportion, 14%, is used solely for the purpose of generating a total excess of approximately 10,000 retirements.

Table 4 : Estimated Payroll Savings Based On  
Increased Retirements of 10,000;  
20,000; 30,000; and 40,000  
Retirements

<u>Number of Retirements</u> <u>In Excess of Normal</u> <u>Rate*</u>	<u>Payroll</u> <u>Savings</u> (000)
10,000	\$171,349
20,000	342,698
30,000	514,047
40,000	685,396

\*assumes equal rates of increase in  
retirements among all eligible classes  
of city employment.

ALTERNATIVE 1:

A supplemental pension of \$500 per year will be paid to each member who retires during the incentive time period. The benefit will be paid annually for the lifetime of the retiree.

The cost of this proposal is shown below based on a normal citywide rate of attrition by retirement of 7200 members per year. Thus, additional payroll savings will be generated by all retirements in excess of 7200: ~~1800 per quarter~~

COSTQuarterly

<u>Number of Retirees</u>	<u>Reserve Required<sup>1</sup></u>	<u>Amortized Cost<sup>2</sup></u>	<u>Net Reduction in Payroll<sup>3</sup></u>
1800	\$ 9,243,000	\$ 495,250	-
2500	\$12,837,500	\$ 687,750	\$ 9,800,000
3750	\$19,256,250	\$1,031,750	\$27,300,000
5000	\$25,675,000	\$1,375,500	\$44,800,000

<sup>1</sup>Reserve required is based on an average retirement age of 63.

<sup>2</sup>The cost of funding the additional reserve is amortized over 35 years at 4% interest.

<sup>3</sup>Average salary is assumed to be \$14,000 per annum.

Projected Retirements In Fiscal Year 1975-76\*

New York City Employees Retirement System	9,000
New York City Teachers Retirement System	3,000
New York City Police Retirement System	2,100
New York City Fire Retirement System	1,100
New York City Board of Ed. Retirement System	<u>250</u>
TOTAL	15,450

\*Projections are based on actual retirements  
in the period July, 1975 through October,  
1975 and reports of the Office of the  
Actuary of New York City.

Table 2: Normal Rates of Retirement

	<u>Actual Retirements In 1973-1974</u>
N.Y.C.E.R.S.	5,590
N.Y.C.T.R.S.	2,275
Police	1,280
Fire	521
Board of Education	<u>251</u>
TOTAL	9,917

ALTERNATIVE 2:

The pension of a retiring member will be increased by 8%.

COST

<u>Number of Retirees</u>	<u>Reserve Required<sup>1</sup></u>	<u>Amortized Cost<sup>2</sup></u>	<u>Net Reduction in Payroll<sup>3</sup></u>
1800	\$10,352,000	\$ 554,750	-
2500	\$14,378,000	\$ 770,250	\$ 9,800,000
3750	\$21,567,000	\$1,155,500	\$27,300,000
5000	\$28,756,000	\$1,540,500	\$44,800,000

<sup>1</sup>Reserve required is based on an average pension of \$7000 per year, and an average retirement age of 63.

<sup>2</sup>The cost of funding the additional reserve is once again amortized over 35 years at 4% interest.

<sup>3</sup>Average salary is assumed to be \$14,000 per annum.

ALTERNATIVE 1:

A supplemental pension of \$500 per year will be paid to each member who retires during the incentive time period. The benefit will be paid annually for the lifetime of the retiree.

The cost of this proposal is shown below based on a normal citywide rate of attrition by retirement of 7200 members per year. Thus, additional payroll savings will be generated by all retirements in excess of ~~7200~~ 1800 per quarter

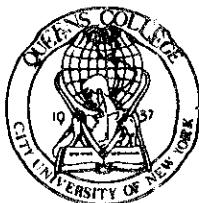
COSTQuarterly

<u>Number of Retirees</u>	<u>Reserve Required<sup>1</sup></u>	<u>Amortized Cost<sup>2</sup></u>	<u>Net Reduction in Payroll<sup>3</sup></u>
1800	\$ 9,243,000	\$ 495,250	-
2500	\$12,837,500	\$ 687,750	\$ 9,800,000
3750	\$19,256,250	\$1,031,750	\$27,300,000
5000	\$25,675,000	\$1,375,500	\$44,800,000

<sup>1</sup>Reserve required is based on an average retirement age of 63.

<sup>2</sup>The cost of funding the additional reserve is amortized over 35 years at 4% interest.

<sup>3</sup>Average salary is assumed to be \$14,000 per annum.



June 23, 1975

The Honorable Robert Weaver  
Director Urban Studies  
Hunter College  
790 Madison Avenue  
New York, New York 10021

Dear Professor Weaver:

Thank you for your kindness in telephoning me today when you have such a tight schedule.

I am sending you several copies of our Resolutions for you to give to members of the Board of MAC if you think desirable. At least it reflects grass-root thinking.

The Report of the State Commission on Public Employees is, of course, excellent but it only touched the tip of the iceberg. May I suggest that the emphasis it places on high pensions is misleading. High pensions are necessary today but the issue is lack of adequate funding, good management, wise investments.

Are you aware that the City has appropriated over \$500 million dollars from the pension funds since last summer to finance expenses of City Hall?

Thank you again for your telephone call and your expert help to secure good management and good protection of our pension money.

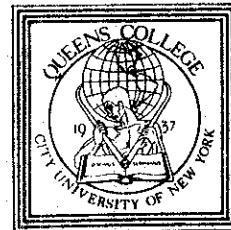
*Mary Earhart Dillon*  
Sincerely,  
Mary Earhart Dillon  
Vice President-Public Relations

45 East End Avenue  
New York, New York 10028

RE 4-1708

# CONFERENCE ON PUBLIC PENSION FUNDS

RESOLUTIONS ADOPTED  
by the Conference held  
on Saturday, April 5, 1975  
at Queens College



Sponsored by  
Queens College Retirees Association



April 23, 1975

Many members of the faculty and retirees are greatly concerned about the safety of pension funds, especially in view of the financial condition of the City. Accordingly we have held a Pension Conference, Saturday, April 5th, and passed eleven Resolutions.

A copy of these Resolutions with supporting material is attached. We hope you will recognize from these Resolutions that something is very wrong with the Pension Systems and that you will appoint a joint committee to investigate and hold public hearings with subpoena power.

We urge you take this action before this session adjourns.

Sincerely,  
*Mary E. Dillon*

Mary Earhart Dillon  
Vice President-Public Relations

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Mary Earhart Dillon  
Wilbur E. Gilman  
Margaret A. Gram  
Glenn W. Howard  
Howard A. Knag  
Ralph G. Ledley

Joseph P. McMurray  
George B. Parks  
George A. Pierson  
Anthony J. Salerno  
Roland M. Whittaker  
William Withers

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## RESOLUTIONS

### RESOLUTION 1. INVESTIGATION

WHEREAS there is widespread concern over the solvency of the New York City pension funds, and  
WHEREAS questionable proposals have been made to use these funds to assist New York City in meeting its general fiscal problems,

THEREFORE BE IT RESOLVED that this Conference requests the Legislature of the State of New York to prohibit further borrowing of pension funds by the City of New York and to appoint an Investment Management Commission of experts to evaluate the soundness of the investment policy of the City on a continuing basis.

### RESOLUTION 2. INFORMATIVE REPORTS

WHEREAS the employees covered under the New York City pension funds have not received full, detailed and sufficiently informative statements concerning the investments in these funds, and

WHEREAS they have also not received full, detailed and sufficiently informative statements concerning the investment policies followed in the management of these funds, the reasons for them, and the effects thereof, and

WHEREAS the employees and retirees covered under these funds have the right to receive this information for their protection,

THEREFORE BE IT RESOLVED that the Investment Management Commission be required to recommend an annual reporting system that will provide full, timely, detailed and accurate information to all employees and pensioners covered by these funds, and that the Comptroller of the City of New York and the trustees of these funds be required by law to follow this system of reporting.

### RESOLUTION 3. INVESTMENT MANAGEMENT COMMISSION

WHEREAS the control of investment policy in the City of New York public pension funds has in fact been concentrated in the hands of ONE MAN, the City Comptroller, and

WHEREAS it is inadvisable to place the responsibility for the proper investment of over \$7 billion in the hands of ONE MAN, however well qualified, and

WHEREAS investment policy on this scale requires the advice of a group of experts,

THEREFORE BE IT RESOLVED that the Investment Management Commission, composed of investment experts including the Superintendent of Banking, the Superintendent of Insurance, and the Chairman of the Permanent Commission on Public Employee Pensions Systems, shall meet weekly to survey and analyze investment policy and make recommendations to the Comptroller.

BE IT FURTHER RESOLVED that the Comptroller of the City of New York shall follow such recommendations in the investment of the pension funds, or make public with ample justifications his reasons for not so doing.

### RESOLUTION 4. INVESTMENT POLICY

WHEREAS the funds of the public pension systems have at times been invested in questionable assets, and  
WHEREAS no satisfactory rules appear to have been adopted concerning the exclusion of certain types of investments, or the proportions of the funds to be distributed between various investment assets, and

WHEREAS such rules are essential to maintain the solvency and liquidity of these funds,

THEREFORE BE IT RESOLVED that the Investment Management Commission recommend certain rules of investment policy prohibiting investment in assets regarded as of dubious value to supplement the statutory restrictions now used, and

BE IT FURTHER RESOLVED that these recommendations be made legally mandatory.

### RESOLUTION 5. REPORT ON LOSSES

WHEREAS considerable losses have led to the sale or so-called "dumping" of securities purchased by the City of New York public pension funds, and

WHEREAS insufficient information has been provided concerning the amount, character and reasons for these losses and the decisions that resulted in the sale of the deteriorated assets,

THEREFORE BE IT RESOLVED that the Comptroller of the City of New York be directed to make a full report to the pensioners concerning the amount, character and reasons for these losses and the sale of the assets.

### RESOLUTION 6. BENEFIT GUARANTY CORPORATION

WHEREAS the Federal Government in 1974 enacted a law which provides for the insurance of private pension funds against loss and insolvency by establishing a Pension Benefit Guaranty Corporation, and

WHEREAS the employees of the City of New York are equally in need of having their pension benefits guaranteed, and

WHEREAS it is apparent that mismanagement of public pension funds as well as private can lead to insolvency of pension money,

THEREFORE BE IT RESOLVED that a New York State Public Pension Benefit Guaranty Corporation be established.

### **RESOLUTION 7. STATE GUARANTEE OF PENSION FUNDS**

WHEREAS in recent years the City of New York has suffered from severe financial problems, and  
WHEREAS the insolvency of the City of New York, should it occur, would seriously threaten the solvency of the  
public pension funds, and  
WHEREAS the public pension systems are governed by state laws, and are vitally affected by state legislative  
decisions,  
THEREFORE BE IT RESOLVED that this Conference request the Legislature of the State of New York to enact a  
law to guarantee the benefit payments of the pension systems from the general revenues of the State whether  
or not a New York State Public Benefit Guaranty Corporation is established. This implements Article 5,  
Paragraph 7 of the State Constitution.

### **RESOLUTION 8. ACTUARIAL ASSUMPTIONS**

WHEREAS the solvency of the New York City Public Retirement Systems depends on the soundness of its actuarial  
assumptions, which have not been revised since 1914, and  
WHEREAS the actuarial assumptions used by the Public Retirement Systems are not generally published, and  
WHEREAS the said actuarial assumptions appear to be invalid in a number of critical respects,  
THEREFORE BE IT RESOLVED that a committee of independent actuaries be engaged to examine the actuarial  
assumptions now used by the Public Retirement Systems in determining the size of the public pension fund  
provided by the City to meet the obligations of the Public Retirement Systems, and be it  
FURTHER RESOLVED that except as may be required by Federal or New York State constitutional or statutory  
provisions protecting members of the Public Retirement Systems, the actuarial assumptions used by the Public  
Retirement Systems be made accurate and be regularly monitored, and that these changes be published  
periodically.

### **RESOLUTION 9. CURRENT FUNDING**

WHEREAS the soundness of the Public Retirement Systems depends on the funding of these Systems being based  
on sound actuarial assumptions, and  
WHEREAS the fiscal soundness of the Retirement Funds depends on adequate funds being provided to it currently,  
and  
WHEREAS the City of New York provides funds to the Retirement Systems on a delayed basis which promises  
potential bankruptcy for the employer without any compensating security for the employees,  
THEREFORE BE IT RESOLVED that the City of New York be directed to fund the Public Retirement Systems on  
a current actuarial basis as soon as possible.

### **RESOLUTION 10. INDEPENDENT AUDIT**

WHEREAS the fiscal solvency of the Public Retirement Systems requires independent audits in order to verify the  
adequacy of its financial operations and the financial statements issued by it, and  
WHEREAS security is of paramount importance to the members of the pension systems,  
THEREFORE BE IT RESOLVED that independent certified public accountants be engaged to conduct annual  
audits of the financial records and statements of the Public Retirement Systems, and that these be made public  
promptly.

### **RESOLUTION 11. PET BANKS**

WHEREAS Chapter 985, Section 178a of the laws of the State of New York of 1972 authorizes the Comptroller of  
the City of New York to deposit funds and securities with local banks for safe keeping, and  
WHEREAS these banks are designated entirely by the Comptroller and in fact become his patronage,  
THEREFORE BE IT RESOLVED that the naming of such banks be made only upon the recommendation of the  
Investment Management Commission, and that the interest and/or fees in such matters be the standard rate of  
the market, and  
BE IT FURTHER RESOLVED that the list of such banks be a matter of public record.

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PENSION CONFERENCE  
SPONSORED BY  
THE QUEENS COLLEGE RETIREES ASSOCIATION

TABLE 9\*

Actual and Assumed Average Salary  
Increases, New York State and  
City Retirement Systems

<u>New York City Retirement Systems:</u>	<u>Actual Annual Average Salary Increase</u>	<u>Assumed Annual Average Salary Increase<sup>5</sup></u>
Employees <sup>1</sup>	6.2% <sup>1</sup>	1.0% <sup>6</sup>
Teachers <sup>1</sup>	7.2% <sup>2</sup>	2.4%
Police	9.1% <sup>2</sup>	1.5%
Fire	9.1% <sup>2</sup>	1.6%
Board of Education	6.1% <sup>1</sup>	1.3%
 <u>New York State Retirement Systems:</u>		
Employees <sup>1</sup>	5.4% <sup>3</sup>	4.7%
Police and Fire	8.8% <sup>3</sup>	3.2%
Teachers <sup>1</sup>	7.5% <sup>4</sup>	2.8%

<sup>1</sup> Based on annual average increase for 1969-1973.

<sup>2</sup> Based on annual average increase for 1970-1974.

<sup>3</sup> Annual average compound growth as indicated by total increase in average salaries between 1969 and 1974.

<sup>4</sup> Estimated from unpublished data furnished by New York State Teachers' Retirement System.

<sup>5</sup> Average of rates for men in age groups 25-55, 30-55, and 35-55.

<sup>6</sup> Clerks.

When actual salary increase is greater than assumed salary increase, results are unfavorable. When actual salary increase is less than assumed salary increase, results are favorable.

\*Table taken from report of the New York State Permanent Commission on Public Employee Pension Systems.

career but are not received until the employee retires. For this reason, it is theoretically possible for an employer to adopt a retirement plan and not make any contributions to it until employees actually begin to retire. This funding approach, known as "pay-as-you-go," is at one extreme of possible funding methods. Obviously, this method is initially inexpensive for an employer who has just introduced a retirement program and who has a relatively young work force. However, its initial advantage becomes a major drawback with the first large wave of retirees. At this stage, the employer is faced with disproportionately large outlays. Woe to the employer -- and his employees -- who has no fund to draw upon to meet benefit commitments that have accrued throughout the years. And if he be a public employer -- woe to the taxpayer.

This need to build up a reserve fund during the early years of a retirement plan to meet subsequent commitments explains why so few pay-as-you-go arrangements can be found. Such a funding technique promises potential bankruptcy for the employer without any compensating promise of retirement security for the employee. As a result of the enactment of the Federal pension reform legislation in 1974, such arrangements are no longer permitted in private industry plans. Sound accounting practices also dictate that costs be reflected at a time when an obligation is incurred, whether the liability will be discharged immediately or at a much later date.

STATE OF NEW YORK  
PERMANENT COMMISSION ON PUBLIC EMPLOYEE PENSION AND RETIREMENT SYSTEMS

Otto Kinzel, Chairman; Joseph G. Metz, Executive Director  
(212) 759-3342

FOR RELEASE: ON DELIVERY

In a report to the Governor and Legislature released today, the Permanent Commission on Public Employee Pension and Retirement Systems warned that the financial soundness of the New York City public employee pension systems is in jeopardy unless corrective action is taken immediately.

By 1977, only two years from now, there will be no assets in the New York City Employees' Retirement System and the New York City Teachers' Retirement System which could be allocated to cover the liabilities for benefits already earned by active members - those not yet retired. The Commission explained that the assets will not be sufficient to cover the amount that should be set aside for retirees at that time. In such event, the systems can no longer be certified as being actuarially sound as required by law.

The Commission also found that the City Fire Department Pension Fund is no longer actuarially sound, and that its deficit has sharply increased from \$166 million in 1969 to \$380 million in 1973 -- a deficit equal to over 80 percent of its total 1973 assets. 1974 figures will show an even greater deficit.

Commenting on the study, Commission Chairman Otto Kinzel stated:

"New York City pension funds are in dire straits. The financial condition of New York City's pension systems has been steadily deteriorating in recent years. This doesn't mean that pensioners or even those who will be retiring in the next few years will not receive their pension checks each month. But it does mean that the City's pension liabilities will continue to outpace the increase in assets, unless there is a major reform in the way these systems are financed. And, if such reform doesn't occur, the future drain on the City budget necessary to insure that pension benefits are not imperiled will be far larger than present forecasts suggest.

"Data from the State Insurance Department incontrovertibly show that the available assets as a percentage of liabilities for active members who have not yet retired from the New York City Employees' Retirement System have dropped from 50 percent in 1967 to an incredibly low 13 percent as of June 30, 1973.

"The City Teachers' System is in even greater danger, financially speaking. In that system, the same ratio of assets, or reserves, to liabilities has dropped from 40 percent to an almost unbelievable 9 percent - a decrease of over 77 percent, while liabilities for active members have increased more than 300 percent to a peak of \$4.2 billion."

The report cites six instances of fiscal "gimmickry" resulting in specific underfunding of the City pension systems by approximately \$2 billion during a period from 1967 to 1975.

The Commission's study, dealing with actuarial assumptions and funding policies of the eight public retirement systems in the State, concluded that the three statewide systems (outside of the City of New York) have generally adhered to the "fully funded" concept on which they were established and are keeping their actuarial assumptions relatively current.

In contrast, the Commission emphasized, the actuarial assumptions used in computing pension costs in the five New York City systems are "...out of touch with reality." "Amazingly," the Commission stated, "the assumptions used for the New York City Employees' Retirement System were prepared for a 1914-18 Commission on Pensions from the City's records of experience from 1908 to 1914 -- more than half a century ago." The use of such flagrantly obsolete assumptions has resulted in a substantial understatement of true public employee pension costs in New York City and, ironically, to ever increasing costs to the City's taxpayers in order to finance the liabilities as they come due. The deterioration has been so great as to raise a question of a possible violation of the guarantee against "impairment" of retirement benefits contained in the State Constitution.

In order to come to grips with these problems, the Commission has recommended a program to assure the adoption of realistic actuarial assumptions and a means of providing the Governor, the Legislature and others concerned with more accurate fiscal information regarding proposed benefit changes. These recommendations will assure more soundly financed programs and a more informed consideration of any proposed benefit improvements.

The Permanent Pension Commission was created by the Legislature and Governor in 1971 in response to unreasonable pressure and demands for further enriched public employee pension benefits and the spiraling costs of the public pension programs. The Commission's purpose is to promote adequate, uniform and equitable benefits for public employees consistent with taxpayer capacity. In its report, the Commission stated that its findings and recommendations should be viewed against a backdrop of annual taxpayer contributions for public employee retirement benefits, including Social Security, which are approximately \$3 billion in 1974-75, an amount double the 1970-71 costs.

The investment advisors furnish the Comptroller, as well as his Investment Advisory Committee and the boards of trustees of each retirement system, various monthly and quarterly reports and schedules reflecting the position and performance of the portfolios. Of course, the Comptroller continues his supervision and retains the final decision and responsibility at all times.

It is worthy of note that for the period September 30, 1971 to June 30, 1972, during which period our present investment advisors were servicing the pension fund systems' common stock portfolios, the time-weighted rate of return on their combined common stock portfolios was 13.29% exclusive of dividend income. This compares with a return of 8.95% and 4.72% respectively, by the Standard & Poor's 500 Index and the Dow Jones Industrial Average.

The Bureau of Investments is headed by Mr. Melvin N. Lechner who was appointed Third Deputy Comptroller on June 14, 1971. Mr. Lechner is a Certified Public Accountant. He has had wide administrative and operating experience, involving financial, accounting, investment and corporate matters, and was at one time associated with the accounting firm of Arthur Andersen & Co.

## Investment Activity

### During 1971-1972

During the fiscal year 1971-1972 my office invested in bonds and mortgages, on a long term basis, \$339.4 million on behalf of the several retirement systems, with an average yield of 7.33%.

A breakdown of the investment activities of all systems for the year ended June 30, 1972, is as follows:

	AMOUNT (In Millions)	PER CENT
Corporate Bonds .....	\$229.8	67.7
Mortgages .....	36.2	10.7
Miscellaneous Obligations ( <i>World Bank \$14.9 million, Canadian \$27.7 million and various U. S. Government Agencies \$30.8 million</i> ) .....	73.4	21.6
	\$339.4	100.0%

## Common Stock Program

Our investment counsellors and Investment Advisory Committee continue to advocate an investment program of dollar cost averaging of the purchase of common stocks of the country's major corporations. It is the belief of our investment counsellors that the economy in 1973 will improve and that the purchases made in 1972 should appreciate.

During the period from July 1, 1971 to June 30, 1972, the Police, Employees' and Fire systems made investments in common stocks of \$126,300,000, \$120,000,000 and \$43,800,000 respectively.

As of June 30, 1972, the market value of common stock investments amounted to \$800.2 million and exceeded cost by \$113.4 million.

The common stock holdings of each of the Retirement Systems, as of June 30, 1972, including the cost and market value thereof, are shown in Table XIV on pages 30 through 32 of this report.

# Statutory Restrictions on Common Stock Investments

The statutory restrictions which are placed upon stock investments by the pension funds are as follows:

1. Stocks must be those of domestic corporations.
2. Stocks (except for stocks of certain qualified banks or trust companies, qualified casualty or fire insurance companies and certain other specified categories) must be listed on a national securities exchange registered with the Securities and Exchange Commission.
3. Stocks must have a record of dividends paid for a period of five years preceding the date of the investment and the earnings during such period shall have been at least equal to the amount of dividends paid.
4. Not more than 3 percent (New York City Employees' Retirement System) and 2 percent (New York City Police, Article 2 and New York City Fire, Article 1-B) of the total issued and outstanding equity securities of any one corporation may be owned by each pension fund.
5. Not more than 1 percent (New York City Employees' Retirement System) and 5 percent (Police, Article 2 and Fire, Article 1-B) of the assets of each pension fund may be invested in the securities of any one corporation and its subsidiaries.
6. Subject to an exception formula, the maximum amount invested in equities in any one year shall not exceed 6 percent of the assets of the New York City Employees' Retirement System.
7. Not more than 30 percent (New York City Employees' Retirement System) and 50 percent (Police, Article 2 and Fire, Article 1-B) of the assets of each pension fund may be invested in equities.

Under legislation sponsored by the Comptroller and enacted during 1970, an extensive bond switching program is being carried on. Low yielding municipal and U.S. government securities held by the pension funds are being sold. These bonds had been purchased in the past, when the interest rates were low. Since the tax exemption feature of municipal bonds is of no value to the tax-exempt pension funds, these bonds may be sold, as market conditions permit, to advantage to individuals and firms desiring this tax exemption. The proceeds are then invested in higher yielding high grade corporate securities. In addition, the advantages of these switches are: (1) it increases the diversification of the fund and (2) under this legislation, the losses on these sales are amortized over a period of twenty years. These losses are more than offset by the investment of the proceeds in higher yielding corporate bonds. During the period ended June 30, 1972, about \$192 million market value of municipal and U. S. government bonds were sold, including the sale on July 6, 1972 of \$162,266,020 of low yielding New York City bonds, and corporate bonds were purchased with the proceeds. This activity resulted in an increase in earnings of the pension systems of about \$5.7 million.

In addition we have been taking advantage of the high interest rates in the bond market by selling low-yielding corporate bonds and reinvesting the proceeds in higher yielding, comparable quality, bonds. During the fiscal year ended June 30, 1972 approximately \$104 million principal amount of corporate bonds were sold, yielding approximately 6.82% and the proceeds were reinvested at a yield of approximately 7.20%.

The First National City Bank continues to act as our bond advisor for the sales and purchases of bonds for the pension funds.



# Managing New York City's Pension Funds

BY MELVIN N. LECHNER  
*Third Deputy Comptroller, The City of New York*

*Before joining the Comptroller's office, the author was with Arthur Anderson & Co., Certified Public Accountants, and Investors Overseas Services. He was awarded a B.A. in Economics from Columbia College, and an M.B.A. in Accounting from the New York University Graduate School of Public Administration. He is now working toward a Ph.D. at NYU's Graduate School of Public Administration. Mr. Lechner is a C.P.A.*

THE NEW YORK CITY Retirement Systems consist of five pension funds — Employees; Teachers; Police — Article 2; Fire — Article 1-B; and Board of Education — which funds have assets of \$6.2 billion. These funds are currently invested to the extent of \$950 million in Equities; \$150 million in U.S. Government Bonds; \$325 million in Mortgages; \$870 million in N.Y.C. Obligations; with the balance of \$3.9 billion in various bonds, ranging from industrials and utilities to Canadians, World Bank, and private placements.

State pension funds in the United States currently have assets approximating \$48 billion. Major Local pension funds have assets of \$12 billion. Thus, the \$6.2 billion of investments by the New York City Retirement Systems represents 10% of the \$60 billion of State and major Local pension funds in the United States.

The responsibility for each of the pension funds rests with the respective boards of trustees of the retirement systems. Each of these boards has delegated the investment management function to the Comptroller of the City of New York, who thus has the responsibility for managing all \$6.2 billion of pension fund assets. In addition to the \$6.2 billion, the Teachers' Retirement System itself manages \$900 million of equity investments for the Teachers' Variable Annuity Fund.

The laws and regulations governing the investments of the N.Y.C. Retirement Systems are contained in the

State Banking Law which is amended by the New York State Social Security and Retirement Law, and the Administrative Code of the City of New York.

## Investment Advisory Committee

Comptroller Abraham D. Beame established and appointed an Investment Advisory Committee which enables the Comptroller to obtain the best possible investment advice. The members are not compensated for serving on the Committee. Chairman of the Committee is Robert E. McNeill, Jr., former chairman of the board and now a director of Manufacturers Hanover Trust Company; the Vice-Chairman is J. Victor Herd, chairman of the Investment Committee of the Continental Corporation. The other members are R. Manning Brown, Jr., chairman of the board of the New York Life Insurance Company; Earl Harkness, a former chairman of the board and now consultant to the Greenwich Savings Bank; Joseph A. Kaiser, president of the Williamsburgh Savings Bank; and George Roeder, vice-chairman of the board, Chase Manhattan Bank, N.A.

The Investment Advisory Committee meets approximately four times a year. At the meetings, the general economic situation, including the bond and stock market outlook, are reviewed. The purchases and sales of the securities of the pension funds are examined and the cash flow allocations are discussed. Each investment advisor reports periodically to the Committee. Mortgage investments are approved by the Mortgage Committee of the Investment Advisory Committee. This Mortgage Committee consists of Messrs. Brown, Harkness and Kaiser.

Until June 1972, all securities were required to be registered in the name of the Comptroller of The City of New York, as custodian for the respective City pension funds. This prohibited registering securities in the name of the advisor, his nominee or broker

name. The Comptroller was also required to maintain physical custody of these securities.

## Custodian Bank

In 1971, Comptroller Beame sponsored legislation to permit the use of a custodian bank to maintain physical possession of the pension funds' securities. Although this proposed legislation did not gain the approval of the State Legislature in 1971, it was subsequently passed in 1972 and signed into law by the Governor.

The utilization of a custodian bank has definite advantages, namely:

1. Theft of securities would be the concern of the Custodian Bank.
2. Collection of dividend and interest income would be the responsibility of the Bank.
3. Sale of securities would be facilitated by having securities registered in the Bank's nominee name.
4. Receipt and delivery of securities by the Comptroller's Office would no longer be required.
5. Personnel in the Comptroller's Office could be reassigned to other functions.

## Equity Investments

Equity investments (\$950 million market value) are restricted to securities that are listed on either the New York or the American Stock Exchanges. In addition, the company must have paid a dividend in each of the last five years.

Four investment advisors manage unequal portions of the equity portfolio. They are First National City Bank, Bank of New York, United States Trust Company and Alliance Capital Management Corporation. These advisors were selected after a long process in which bids were received from over thirty financial institutions.

During the past twelve months, the advisors have performed fairly well.



THE CITY OF NEW YORK  
OFFICE OF THE COMPTROLLER  
MUNICIPAL BUILDING  
NEW YORK N.Y. 10007

ABRAHAM D. BEAME  
COMPTROLLER

# NEWS

FOR RELEASE: IMMEDIATE RELEASE  
WEDNESDAY, December 6, 1972

72-237

Comptroller Abraham D. Beame announced today that the common stocks held by the New York City retirement systems enjoyed a "dramatic" 16. 81% increase in value for the 12-month period ending September 30, 1972.

Mr. Beame compared the 16. 81% increase in value with increases of two other indices: the Dow Jones Industrial Average, which went up 7. 45% in the same period of time and Standard & Poors 500, whose increase was 12. 42%.

Mr. Beame, as Comptroller, has the responsibility for investing the \$6. 2 billion of assets of the City's five pension systems. Investments include, among others, U. S. Government bonds, corporate bonds, mortgages and common stock.

In deciding how he will invest pension funds, Mr. Beame receives advice from an Investment Advisory Committee which he created and specific recommendations from four Investment Counsellors.

The Comptroller said all increases were computed on a time-weighted rate of return basis. A time-weighted rate of return, a method of performance computation which is standard in the financial world, has to be used in this case, because approximately \$19 million of new cash was invested in equities every month. A simple computation of a 12-month increase in the value of holdings in the pension systems would not be valid.

# City Pension Fund a Model of Mishandling

By WILLIAM SHERMAN

(First of a series)

The city employees' \$7 billion pension fund, long hailed as a model of security and high profits, has been earning less than savings-bank interest for nearly 20 years.

Last year, the fund suffered a \$162 million loss in its \$1 billion stock portfolio and an enormous depreciation in its \$5 billion bond holdings.

The impact on the taxpayer, now picking up the \$1 billion annual tab for a long history of poor management by the fund's managers is just beginning to emerge.

Consistently poor returns on investments have raised serious doubts as to whether the city could meet its soaring retirement obligations in the future without placing an unbearable burden on the taxpayer.

In the last two years, the annual cost to the taxpayer for city pensions has jumped from \$465 million to an estimated \$1,075 billion for 1974-75 as the first shock wave of sharply in-

**Taxpayers will pay \$1 billion in fiscal 1974-75 toward the cost of pensions for city employees, an increase of more than 100% over two years ago.**

**Last week, Mayor Beame disclosed that the skyrocketing pension tab, a major cause of the current \$1.5 billion budget gap, might very well result in higher income and real estate taxes for city residents.**

**Why? An investigation by The News has disclosed that today's taxpayer is paying for more than 40 years of poor management and poor investment policy by the managers of the city's pension fund. The years of neglect and the transfer of yesterday's pension cost to today's taxpayer are finally hitting home.**

assets of the fund to buy up much of the city's debt in the form of low-yielding, tax-free municipal bonds.

Since the pension fund was automatically tax free, there was no financial advantage in purchasing the city's obligations. During most of those years, corporate bonds and other investments were yielding up to twice as much as the city bonds. In effect, the controllers were using the assets of the pension fund to help support the city.

## 66% Tied Up in City Bonds

By 1961, when Abe Beame, then the controller, decided to stop buying the municipals, more than \$1 billion, or 66%, of the fund was tied up in city bonds earning less than 3.2% interest a year.

The only way to improve the fund's earnings was to sell the municipals and use the proceeds for investment in higher-yielding securities. Although he sold some of the bonds in his first term, it was not until 1971, that Beame and his new deputy controller, Melvin Lechner, began to unload the old municipals on a large scale.

By that time, other tax-free bonds

in the private sector were earning as much as 18%.

And the fund's recent \$1 billion stock investment has barely earned 1.5%, including dividends in the last three years, while the average private fund's equities, according to one survey, have earned 15%.

Since 1921, when the fund was established, it has been managed by representatives of the city, its various member unions, and private citizens with backgrounds in financial affairs. The city controller directs the investment of the fund's assets.

For 40 years, the controllers passed up opportunities to buy high-yielding corporate bonds and instead, used the

(Continued on page 47, col. 3)

## EMPLOYEES' FUNDS TO BUY CITY NOTES

1/4/75

**\$425-Million to Be Invested in First Quarter of 1975 in a Private Placement**

By VARTANIG G. VARTAN

New York City's employee pension funds and sinking funds plan to invest an estimated \$425-million during the first quarter of 1975 in a private placement of city notes.

This move, unprecedented in recent years, is being preceded by smaller investments in the secondary, or trading, market for short-term city notes by various trust funds under the controller's jurisdiction.

Ironically, the decision to buy city note issues comes not long after completion of a program to eliminate New York City bonds — having much longer maturities than notes — from pension fund portfolios.

### Investing Confirmed

In commenting yesterday on Wall Street reports, William T. Scott, deputy controller for money management, confirmed that the city's pension and sinking funds will invest between \$400-million and \$450-million in new notes, with actual purchases targeted for mid-January and mid-March.

"In addition," Mr. Scott said, "we bought almost \$5-million of existing city notes, maturing from a few days to several months, in the secondary market between Dec. 20 and Dec. 31.

"An attempt will be made by the Controller's office to make further meaningful purchases in the secondary market by the trust funds."

Meanwhile, there were reports in Wall Street that another purchase of existing city notes of around \$5-million was made yesterday. The Controller's office had no comment on this.

The large infusion of city capital now in prospect for mid-January and mid-March has the effect of leveling the borrowing schedule of New York for the remainder of the fiscal year ending June 30.

This meeting followed a near-vote placement was the result of a Dec. 17 meeting that involved Mayor Beame, Controller Harrison J. Goldin and members of the financial community who advise the city on its debt management.

This meeting followed a near-disastrous decline in New York City securities amid fears that the municipal market would not be able to absorb the huge supply of city offerings then in prospect.

### \$620-Million of Notes

As a result, the city's only contemplated new issue this month is \$620-million of notes (all notes mature in less than one year) next Tuesday. A contemplated January bond issue of perhaps \$500-million was replaced by plans for a \$140-million bond issue in February.

At present, the schedule also calls for a bond issue of \$500-million in April. Notes will be issued from February through June, according to the prospective schedule, at the rate of \$550-million a month.

The Controller's office administers the city's five pension, or retirement, funds as agent for the various retirement boards. It also administers the several sinking funds.

In addition, the office supervises the investments of such

## EMPLOYEES' FUNDS TO BUY CITY NOTES

Continued From Page 29

trust funds as the Staten Island Memorial Fund, the Urban Development Corporation account and the Securities Deposit Account. The latter consists of money put up by contractors on city projects to serve as performance bonds.

One Wall Streeter commented yesterday that the investment of city funds in notes makes sense in that the money is tied up for only a relatively short period and not "locked up" in long-term bonds. In addition, he said, the present yield on the city's tax-exempt notes is competitive with various taxable obligations.

Following the mid-December decision to trim the size of debt offerings, New York City's obligations rallied somewhat in price.

## THE NEW YORK TIMES

## GOLDIN CAUTIONS ON CITY FUND AID

Warns Not to Rely on U.S. and State to Fill Gap

2/25/75

Controller Harrison J. Goldin cautioned yesterday that the city should not rely on "massive amounts of new revenue from the Federal and state governments" to fill a budget gap for the coming fiscal year, which begins July 1.

The Controller said he fully supported the Mayor's drive to obtain an additional \$880-million in outside assistance, but said "all indicators" showed that the sum might not be forthcoming.

"Part of the fiscal trouble we are now in stems from past expectations of Federal help which did not materialize," he said. "We must get on with the task of effecting the stringent economies in operation, which are as essential as they are painful."

The Controller's statements, in a luncheon speech to the Queens Chamber of Commerce at Riccardo's Restaurant in Long Island City, were seen as a mild rebuke to Mayor Beame.

Eleven days ago, in forecasting a deficit of \$1.68-billion in a budget of more than \$12-billion for 1975-76, the Mayor said he hoped for an additional \$883.8-million in Federal and state aid.

Mr. Goldin praised the Mayor for his efforts to deal with a deficit in the current budget by laying off city employees and halting some capital construction projects.

"It will not be easy to make further cuts, but it must be done," he said.

The Controller also said that he was opposed to the principle of issuing budget notes to cover the current deficit, which he termed "only salting the wounds."

## STATE HELPS EASE CITY FISCAL PINCH

2/25/75

New Law Widens Investing of 4 Sinking Funds to Allow Meeting of Payroll

By ALFONSO A. NARVAEZ  
Special to The New York Times

ALBANY, Feb. 24—Governor Carey today signed into law emergency legislation, passed earlier today by both houses of the Legislature, designed to help New York City meet payroll and operating expenses that become due by the end of the week.

The measure, which passed in the Assembly by a vote of 103 to 41 and in the Senate by 47 to 10, amends the City Charter to delete a requirement that the Controller invest sinking fund money in city bonds when they are available at below par.

The measure passed both houses shortly after 5 P.M., and a facsimile was transmitted to the Governor, who signed it in his New York City office, where he is seeking a solution to the fiscal woes of the Urban Development Corporation.

Opponents in both houses of the Legislature argued that the measure was another step toward the "deregulation" of the city. Opponents argued that the city would be able to save millions of dollars.

### Flexibility the Goal

The measure is designed to give the Controller flexibility in investing the more than \$958-million in the city's four sinking funds. The funds date to 1898 and are separate accounts that grow with yearly contributions from the city's general treasury; they are used to redeem and retire long-term city debt.

Last Friday the City Council passed a home-rule message requesting the Legislature to approve the Charter change. Basically it will allow the Controller to use funds to purchase \$200-million in city notes directly from the city's pension programs, which purchased them last month at about 7.5 per cent interest.

The pension programs will receive \$204-million for the notes and will add \$41-million to this to buy a new \$245-million issue of city securities being put on sale tomorrow. The city needs the money to meet operating expenses, including payrolls due on Friday.

Senator Jeremiah Bloom, Democrat of Brooklyn, said that the measure would save the city about \$3-million—or \$1-million that would have had to be paid as brokers' fees if the notes were sold on the open market and \$2-million in interest.

The Senate majority leader, Warren M. Anderson, Republican of Binghamton, said that if the measure would save the city some money, "it would be ridiculous to oppose it."

But opponents argued that the investment restrictions were wise restraints. Senator John J. Santucci, Democrat of Queens, said the bill amounted to "fiscal folderol."

TO: Governor Carey  
FROM: Donna Shalala  
SUBJECT: Financing New York City's Employee Retirement System

This draft memorandum was prepared at your request. The research was conducted under my direction by Dr. Bernard Jump visiting professor of economics at Syracuse University. He is the leading expert on the state and city pension systems.

A single question is answered in this analysis: What are the implications if New York City were authorized to depart from its traditional practice of prefunding for retirement benefits earned by City employees and to substitute in its place a pay-as-you-go (PAYG) approach.

A. There would be an immediate expenditure reduction. For a few years this reduction would be around \$500 million.

A precise estimate of both the size and duration of potential expenditure reductions will require considerable computer work. However, the attached table which summarizes the assets and payments of the five City actuarial retirement systems confirms this point. Currently the total of employee and employer contributions and investment income exceeds benefit payments by several hundred million dollars.

B. Despite the attractiveness of using such funds to solve the current crisis such a step is not recommended. The major reasons for such a recommendation are:

RECEIPTS, PAYMENTS, AND ASSET HOLDINGS OF NEW YORK CITY'S  
ACTUARIAL RETIREMENT SYSTEMS, 1970-1974

(Dollar Amounts in Millions)

Fiscal Year Ending	Employee Contri- butions	Employer Contri- butions	Interest and Dividend Income		Total Receipts (Col 1 + Col 2 + Col 3)	Benefit and With- drawal Payments	Assets Held at End of Year	Benefit/Asset Ratio (Col 5- Col 6)
			(1)	(2)				
1970	\$130	\$ 383		\$246	\$ 759	\$367	\$5,693	6.4%
1971	172	484		273	929	463	5,941	7.8
1972	191	449		313	953	537	7,011	7.7
1973	173	503		339	1,015	677	7,265	9.3
1974	192	751		385	1,328	694	7,742	9.0
1975				716				
1976				1,021				
1977				1,100(E)				
1978				1,110(E)				
1979				1,115(E)				

Source: All Data Except Those For Employer Contributions Are From U. S. Bureau of the Census, Finances of Employee-Retirement Systems of State and Local Governments (Selected Years) and Census of Governments, 1972, Vol. 6, Topical Studies, No. 1, Employee Retirement Systems of State and Local Governments. Employer contribution data are from official New York City records.

(E) - Estimate.

To: The Honorable Hugh L. Carey, Governor

2.

1. Despite annual City expenditures to finance retirement systems that now exceed \$1 billion annually, New York City's pension obligations to current and retired employees have been growing more rapidly than have assets accumulated to back these liabilities. Moreover, if the City retirement systems were complying fully with the intent of the law and using realistic actuarial assumptions, annual City contributions would be \$200-\$300 million higher.

2. Owing to a long-standing impasse between the City and members of the system with respect to the meaning of the funding legislation, the Fire Department Pension Fund is likely by the early 1980's to be without sufficient funds to meet all obligations owed. At the moment the system is actuarially insolvent and the size of its insolvency is growing rapidly. Even if the current funding method is retained, the Fire system is soon going to require substantial infusions of money over and above those contemplated under present financing schedules.

3. Despite the appearance that New York City's retirement systems are awash with surplus funds which obviate the necessity of continuing City contributions at current levels, the facts are very much to the contrary. Although the systems' current income exceeds benefit payments, the number of retired City employees collecting benefits and the average size of benefit payments will continue to grow at rates that will steadily narrow the gap between systems' income and benefit payments.

4. Actuarial funding of retirement benefits recognizes that the obligations should be paid for when they are incurred just as every other element of employee compensation is paid for as it is earned.

5. Former and current City employees who are now or will eventually be eligible for pension benefits would have good reason to question whether they would get their payments if the systems were financed on a PAYG basis. Since some City employee groups are now objecting to the use of retirement system assets to acquire City and MAC securities, it is likely that they would oppose even more vigorously efforts to revise pension financing methods in ways that would have as a certain outcome the diminishment of system assets.

To: The Honorable Hugh L. Carey, Governor

3.

The New York State Constitution, Article V, Section 7, guarantees that benefits given to members of public employee retirement systems cannot thereafter "be diminished or impaired." To resort to pay-as-you-go financing would definitely impair the security behind pension benefits already credited to former and present employees, whether or not the courts would interpret this as unconstitutional.

6. Only Massachusetts among the states and few large cities operate PAYG retirement systems, though many public systems operated nominally on an actuarially financed basis are severely underfunded. In Washington, D. C., a city-federal commission has concluded that the city's use of PAYG methods to finance police and fire pensions was leading to a "dangerously high" level of unfunded liabilities and recommended that system financing be placed on a sound actuarial basis.

7. Federal legislation enacted in 1974 prohibits PAYG financing of private industry pension plans. Hearings and official studies are now underway to determine whether public pension plans should be brought under federal control. Thus, it is possible that Federal law may eventually prohibit PAYG financing of a public employee retirement system.

8. Because PAYG financing minimizes the immediate costs of most retirement benefit improvements, legislators might find it more difficult to resist pressures exerted by public employee groups to enact benefit improvements.

9. The total cost to New York City to provide a specified package of retirement benefits to a particular employee group would be far greater under PAYG than under actuarial funding because the City would forego under the former approach the opportunity to earn interest on accumulated assets. As observed by a leading authority, "(i)n a mature retirement system operating on a funded basis, the annual income from interest and dividends may equal or exceed the amount being contributed to the fund by the employer."

10. In recent years the investment community has begun to recognize that retirement obligations represent a commitment of a community's financial resources just as conventional indebtedness does. Thus, it is unlikely that

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a move to PAYG pension financing by New York City would be viewed as a positive step toward fiscal reform.

In summary, there are few compelling arguments for PAYG financing beyond the obvious one that New York City could postpone for an undetermined time the need to spend several hundred million dollars. But in no more than a few years at best the City would find itself paying the price for such a postponement. This price would be reflected by the need for rapidly increasing appropriations to finance retirement benefits owed. Despite grossly unsound fiscal practices elsewhere in New York City's operations, the retirement systems, while not entirely free of the effects of fiscal legerdemain, have managed to remain one element of operations that can still be characterized as reasonably secure. It is to be hoped they will be permitted to remain secure.