(This packet was printed on recycled paper.)

Public notice was given to *The Register-Guard* for publication on July 22, 2011.

LANE TRANSIT DISTRICT
BOARD OF DIRECTORS
HUMAN RESOURCES COMMITTEE

Tuesday, July 26, 2011
4:00 P.M.

LTD CONFERENCE ROOM
3500 E. 17th Avenue, Eugene
(off Glenwood Blvd.)

Public testimony will not be heard at this meeting.

AGENDA

I. CALL TO ORDER

II. ROLL CALL

III. Dubick (Chair) ______ Gillespie ______ Kortge ______

IV. FUTURE DESIGN OF LTD PENSION TRUSTS

V. NEXT MEETING

VI. ADJOURNMENT

BOARD HUMAN RESOURCES COMMITTEE
AGENDA ITEM SUMMARY

DATE OF MEETING: July 26, 2011

ITEM TITLE: FUTURE DESIGN OF LTD SALARIED PENSION PLAN

PREPARED BY: Mary Adams, Director of Human Resources and Risk Management

ACTION REQUESTED: None

BACKGROUND:

This Committee has been working toward development of a new pension plan for new salaried employees since February 7, 2011. The last discussion to occur was at the June 13, 2011, Board of Director's meeting. At that meeting Milliman Actuary Pete Sturdivan presented three options for plan design, along with preliminary cost and benefit estimates. Based on that presentation, staff was directed to begin design of a new pension plan for employees hired on or after January 1, 2012. Board members gave staff broad guidelines for a defined contribution plan model paired with a voluntary matching plan. Since that meeting Milliman staff and Everett Moreland, attorney for the retirement plan, have collaborated with LTD staff to prepare a set of additional decisions that need to be made before a final draft plan can be prepared.

Will Clark-Shim, Milliman actuary, and Everett Moreland have prepared documents that address the key decisions to be made. These documents are included in the packet for this meeting. Both Mr. Clark-Shim and Mr. Moreland will be present, along with LTD staff, to share their recommendations regarding these decisions. The intent of this discussion is to give Mr. Moreland enough direction to draft the new plan. If one meeting is not enough time to accomplish this, or if more information is needed by the Board members, additional meetings will be scheduled.

ATTACHMENTS: Retirement Program Redesign presentation, dated June 13, 2011
Letter from Milliman dated July 21, 2011

PROPOSED MOTION: None

Q:\Reference\Board Packet\2011\07\Board HR Committee 07-26-11\AgenSum Future Deisgn of LTD Salaried Pension Plan.docx

LANE TRANSIT DISTRICT

Retirement Program Redesign

June 13, 2011

Defined Benefit Plan

A defined benefit plan is one that provides a definitely determinable monthly benefit at retirement. Typical monthly benefits are expressed as a flat dollar rate per year of service or a flat percentage of final average salary per year of service. Current administrative employees are covered by a final average salary defined benefit plan.

Cash Balance Plan

A cash balance plan is a modified defined benefit plan that expresses benefits in terms of account balances. These plans look like defined contribution plans, because prior to retirement, the accrued benefit is expressed as an account balance based on annual additions to the account and a guaranteed interest rate. Unlike a defined contribution plan, the account does not increase with an allocated share of actual investment income each year, but by a formula rate defined in the plan. Proposal 1 in this presentation includes a cash balance plan component.

Defined Contribution Plan

A defined contribution plan provides a benefit based on the accumulation of pre-determined contributions. For example, the level of annual contribution is specified in the plan; e.g., 4% of pay. Under a defined contribution plan, if an employee quits, dies, retires or becomes disabled, the account balance is normally payable. However, lump sums do not have to be paid and the normal form of benefit may be an annuity purchased from an insurance company. Proposal 2 is a defined contribution only proposal.

Combination of Defined Benefit Plan or Cash Balance Plan with a Defined Contribution Plan

The administrative retirement program is currently made up of a defined benefit plan and a defined contribution plan. This structure can take advantage of good features of both designs, including lifetime benefits and portable benefits. There will be two plans to administer, and must look at both plans when considering benefit levels. Both Proposals include a defined contribution component.

LTD Retirement Benefits

Plan Features	LTD & ATU Local No. 757 Pension Trust	LTD Salaried Employees' Retirement Plan		LTD Deferred Compensation Plan
Type of Plan:	Defined Benefit	Defined Benefit	Defined Contribution	457(b)
Who is Eligible:	ATU Represented Employees	Administrative Employees	Administrative Employees	All LTD Employees
When Established:	1972	1975	1999	1984
Vesting:	100% in Employee Participation Account at three years; 100% in pension at earlier of five years or 60th birthday while an LTD employee	100% at earlier of five years or 60th birthday while an LTD employee	100% immediately	100% immediately
Full Retirement:	Age 60 or 30 years of credited service	Age 60 or 30 years of service	N/A	N/A
Early Retirement:	Reduced benefit at age 55 and five years of credited service	Reduced benefit at age 55 and five years of service	N/A	N/A
Retirement Benefit:	$64 per month per year of credited service	1.67% of Final Average Annual Salary, divided by 12 times benefit credit years; or, if greater, 3% of Final Average Annual Salary divided by 12 times benefit credit years (up to 25), less the member's deemed primary social security benefit at age 62	Full balance taken at retirement	Full balance taken at retirement
Contribution Rate:	$4.26 per hour	18.3% of salary	6% of salary (all from LTD)	Employee deferral
MV Assets, Last Val Date:	$13,900,000	$7,900,000	Individual accounts	Individual accounts
Fund Manager:	RV Kuhns - Consultant	RV Kuhns - Consultant	AIG-VALIC	AIG-VALIC or Hartford
Who Directs Funds:	Trustees	Trustees	Employee self-directs funds	Employee self-directs funds
Trustees:	Four members: two representing ATU, two representing LTD	Three members: Board President, General Manager, Director of Human Resources and Risk Management		LTD

LTD Admin & OPSRP Comparison

Plan Features	OPSRP		LTD Salaried Employees' Retirement Plan	
Type of Plan:	Defined Benefit	Defined Contribution	Defined Benefit	Defined Contribution
Vesting:	Five years of service or age 65	100% immediately	Five years of service or age 60	100% immediately
Full Retirement (DB):	Age 65, or age 58 with 30 years of service	N/A	Age 60 or 30 years of service	N/A
Early Retirement (DB):	Actuarially reduced benefit at age 55 and five years of service	N/A	Reduced benefit at age 55 and five years of service (3% per year from 60 to 58; 8% per year from age 58 to 55)	N/A
Final Average Salary	Base pay, overtime (limited), bonus. No unused sick or vacation time.	N/A	Base pay, overtime, bonus. Includes accrued and unpaid Consolidated Annual Leave.	N/A
Full Retirement Benefit:	1.5% of Final Average Annual Salary divided by 12 times years of service	Full balance or installments taken at retirement	1.67% of Final Average Annual Salary, divided by 12 times benefit credit years; or, if greater, 3% of Final Average Annual Salary divided by 12 times benefit credit years (up to 25), less the member's deemed primary social security benefit at age 62	Full balance taken at retirement
COLA:	Usually 2% per year	N/A	N/A	N/A
Normal Contribution Rate:	6.1% of salary	6% of salary (usually ER-paid); voluntary employee contributions	11.0% of salary	6% of salary from LTD; voluntary employee contributions
Actuarial Cost Method:	Projected Unit Credit	N/A	Entry Age Normal	N/A
Discount Rate:	8.0%	N/A	7.5%	N/A
Mortality:	RP-2000 Healthy White Collar, generational projection	N/A	RP-2000 Healthy	N/A

Previous Board Input

- Current retirement benefits are coming at high cost
- Employee should be responsible for retirement income decision
  - Including whether to purchase guaranteed lifetime income
- Target benefits cost at approximately 9% of payroll

Details of Possible Retirement Program Designs

Retirement Plan	Current Benefit Structure	Proposal 1 – Cash Balance	Proposal 2 – Defined Contribution
Normal Retirement Age (NRA)	Age 60 or 30 years of service	Age 65 and 5 Yrs. of Cr. Svc	Age 65 and 5 Yrs. of Cr. Svc
Normal Retirement Benefit (NRB)	1.67% of Final Average Annual Salary, divided by 12 times benefit credit years; or, if greater, 3% of Final Average Annual Salary divided by 12 times benefit credit years (up to 25), less the member's deemed primary social security benefit at age 62	Amount provided by Account	Amount provided by Account
COLA	None	Depends upon annuity basis	Depends on annuity basis
Annual Pay Credit / Employer Contribution	N/A	**7.0% of pay for first 5 years 8.75% of pay for years 6 - 10 10.5% of pay for years 11 - 15 12.25% of pay for years 16 - 20 14.0% of pay thereafter**	**4.5% of pay for first 5 years 5.6% of pay for years 6 - 10 6.7% of pay for years 11 - 15 7.8% of pay for years 16 - 20 9.0% of pay thereafter**
Interest Crediting Rate	N/A	**4.0% per year**	Based on plan's investment performance
Early Retirement	Age 55 and 5 Yrs. of Cr. Svc	Age 55 and 10 Yrs. of Cr. Svc	Age 55 and 10 Yrs. of Cr. Svc
Unreduced Early Retirement	Age 60 or 30 Yrs. of Cr. Svc	N/A	N/A
Early Retirement Factors (ERF)	3% from 60, 8% from 58	N/A	N/A
Early Retirement Benefit	NRB x ERF (3% for 2 years, then 8%)	Amount provided by Account	Amount provided by Account
Defined Contribution Plan			
Annual Employer Contribution	6% of covered pay	N/A	See above
Matching Formula	N/A	**50% of employee deferral on the first 6% of base salary**	**50% of employee deferral on the first 6% of base salary**

Discussion Points – Defined Contribution

- Defined contribution plans build up an account balance which the employee can roll over to an IRA upon retirement, and spend over the course of a retired lifetime.
- The District provides no guarantees to participants beyond the initial contributions into the account.
- Most defined contribution plans allow participants to direct investments.
- The Board indicated some interest in managing employees' investments up until the time of retirement.
  - Employer-directed investments come with fiduciary responsibilities.
  - Some "traditional" defined contribution plans have taken this approach by investing in, for example, 60% equity / 40% bond "balanced" portfolios.
  - An alternative approach to employer-directed investments might be to invest each member's assets in a target-date fund based upon their stated date of retirement. Target-date funds change asset allocations to more conservative investments as a participant approaches a stated retirement date.

Discussion Points – Cash Balance

- Cash balance plans build up an account balance which the employee can either annuitize or roll over to an IRA upon retirement.
- Must offer at least one annuity benefit
  - Can be for a period certain of 10 years or more, or can be a single or joint life annuity
  - Can offer annuity through an insurance company instead of through the Trust
- If lump sum payouts are offered, they are likely to be taken
- The District guarantees the initial contribution credits as well as all interest credits in the account.
  - The relatively low 4% guaranteed interest crediting rate is offset by higher pay credits.
- Early Retirement Window benefits can be provided within a cash balance plan
- A cash balance plan might stand a greater chance of acceptance from the ATU as the District looks to redesign its hourly employees' benefits.

Replacement Income

Following is a summary of employer-provided monthly pension benefits provided to a hypothetical retiree who is age 62 with 25 years of service. Base annual salary at retirement is $65,000. Benefits under the current DB plan also reflect a Consolidated Annual Leave cashout at retirement of 360 hours.

The current benefit structure also includes District-paid monthly retiree medical benefits of up to $250 prior to age 65, and $125 thereafter. This medical benefit is not included in the benefits and cost analyses on this and the following slide.

	Current Benefit Structure	Proposal 1 – Cash Balance	Proposal 2 – Defined Contribution
Age 62 Monthly Benefits			
-- DB Plan	$2,234	$1,137	$0
-- DC Plan	$879	$0	$952
-- District Match	n/a	$440	$440
-- Total	$3,113	$1,577	$1,392
Monthly Base Pay	$5,417	$5,417	$5,417
Replacement Ratio to base pay			
At retirement	57%	29%	26%
20 years later	33%	17%	15%

Estimated Program Costs

Following is a summary of the costs to the District of sponsoring the retirement benefits previously shown:

	Current Benefit Structure	Proposal 1 – Cash Balance	Proposal 2 – Defined Contribution
% of Payroll Costs			
-- DB Plan*	11.9%	6.5%	0.0%
-- DC Plan	6.0%	0.0%	6.8%
-- District Match	n/a	2.4%	2.4%
-- Total	17.9%	8.9%	9.2%

These costs are based upon data and assumptions stated towards the end of this presentation, and are designed to reflect the expected experience of future salaried employees.

** Costs for the current defined benefit plan are 10.6% of payroll for true new hires, and 14.4% of payroll for ATU transfers. Costs for the cash balance and defined contribution proposals are for transfers and new hires combined, and assume transfers will receive higher accrual rates in observance of ATU service.*

Observations on Benefits and Costs

- Proposals 1 and 2 are designed to cost the District approximately 9% of covered pay, including matching contributions.
- The current benefit structure comes with risks of increasing contributions if Trust investments do not meet the assumed annual return.
- Proposal 1 comes with smaller risk of increasing contributions because the actuarial assumptions are more conservative and the normal cost is lower.
- The current benefit structure is significantly richer than the proposed structures. This may pose challenges for attracting and retaining future employees.
- If the current benefit structure’s DC component could be eliminated or reduced, that would immediately save the District significant revenue and bring greater parity between old and new benefit structures.
- Female members tend to do better than males under defined benefit structures because of their longer expected lifetimes.
- If the cash balance plan does not provide meaningful guarantees to the participants, a defined contribution plan may cost less to administer, would expose the District to less risk, and may be more transparent to employees.

Workforce Management

- Removal of retirement income guarantee, lower level of benefits, and lack of early retirement subsidies could lead to later retirement for future generations of workers.
- Backloaded formula for cash balance and defined contribution plans will help retain workers until retirement, but may also encourage later retirement.
- Current retirement benefits are substantially richer and more secure than proposed retirement benefits. This may lead to communication issues with future hires.
- If current ATU employees are placed into the new retirement benefits upon transfer to salaried employment, it may be difficult to induce employees to transfer.
  - ATU transfers have comprised approximately 35% of new salaried employees over the past ten years. Current ATU employees could transfer into the current salaried retirement benefit structure but the savings of adopting a new retirement benefit structure would be postponed.

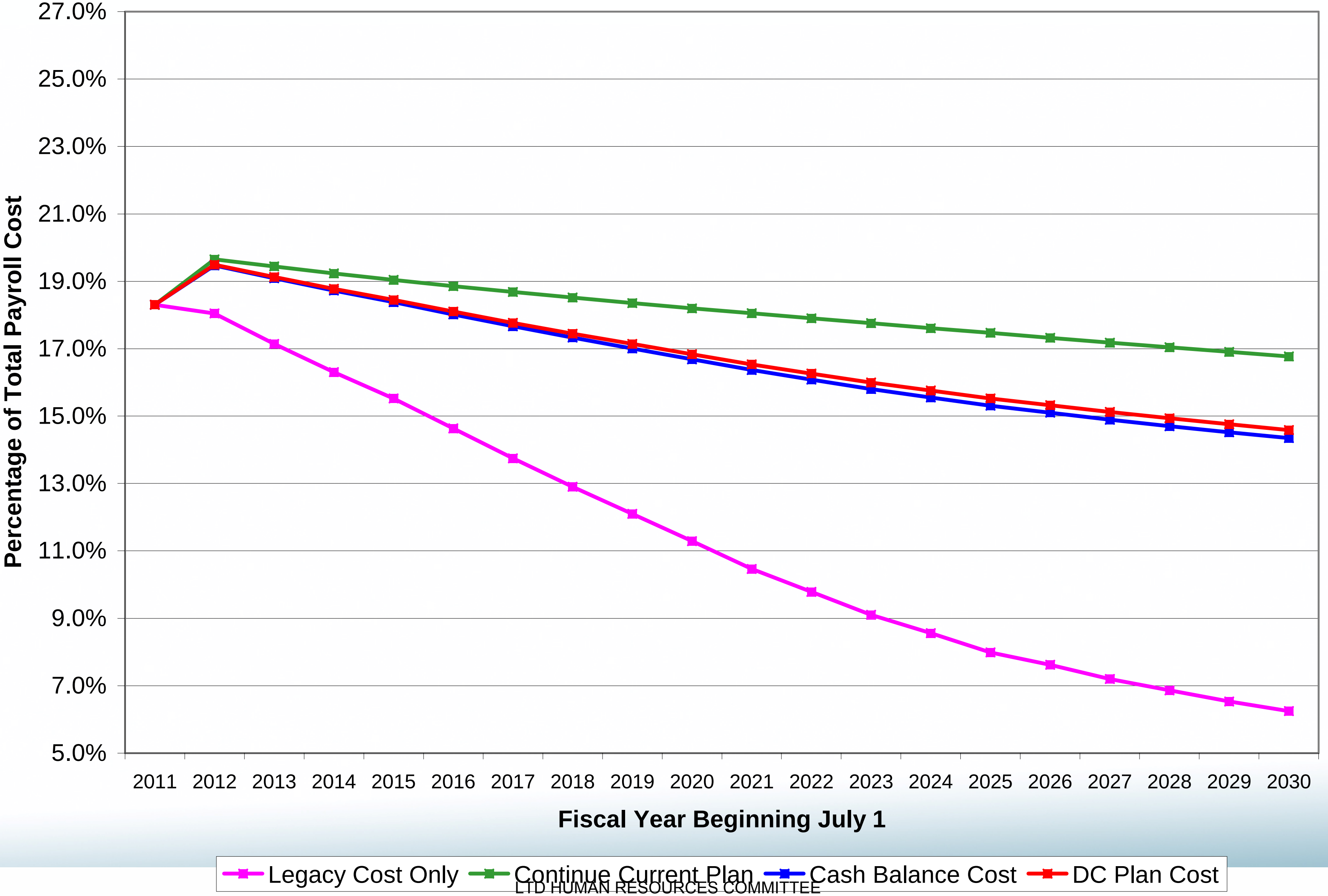
Current Benefits

- Budgetary pressures are a primary reason for pursuing retirement benefits redesign.
- Focus has been on future employee benefits.
  - Retirement Plan Legal Counsel recommends against altering the defined benefit structure for current employees, because of legal uncertainties.
- Reducing or eliminating current employees Part 2 benefit would deliver greater parity between current and proposed benefit structures, and would help satisfy the budgetary goals which have led to the change in benefits
  - Retirement Plan Legal Counsel believes that the "Part 2" 6% of pay defined contribution structure for current employees could be altered or eliminated.

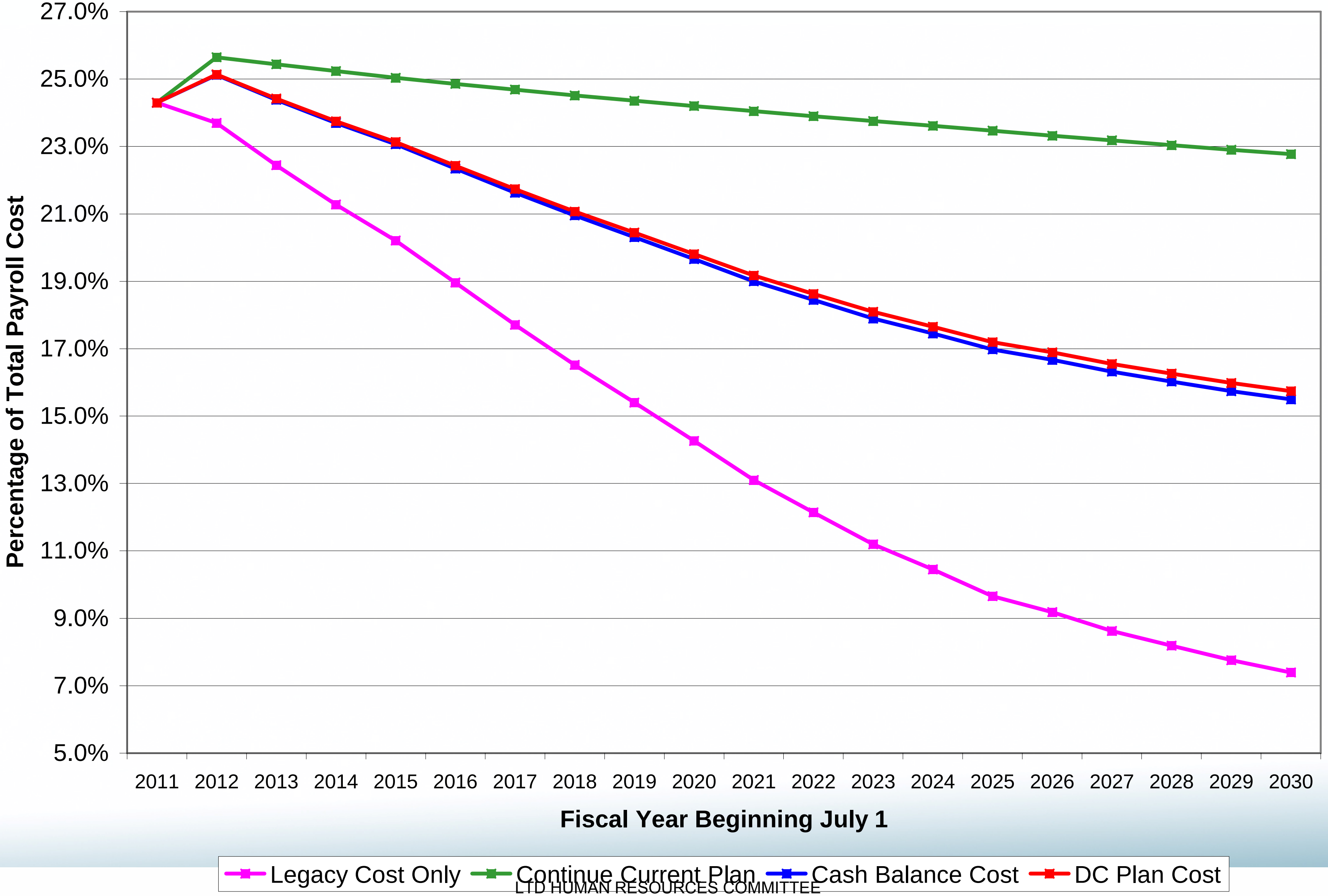
Current Benefits

- Removing future entrants from the current defined benefit structure will put upward pressure on the costs for those benefits.
  - Current GASB rules – which are a benchmark for cash funding – require that unfunded liability be amortized in level dollar installments, not as a level percent of payroll.
    - Switching to level dollar installments generally increases scheduled contributions.
    - However, if a cash balance plan is adopted, a switch to level dollar installments may not be required.
  - As the covered population ages, a shortening investment horizon may lead to more conservative investments and therefore a lower expected rate of return.
  - However, salary increases for the remaining senior population will generally be lower than for the District as a whole.
  - Several potential assumption changes may warrant review for the 2011 valuation.
- The following slide shows a projection of current salaried retirement plan costs for next 20 years as a percentage of total District payroll.
  - "Legacy Cost" – current pension plan for the closed group of participants
  - "Current Plan" – current pension plan, including future participants
  - "Cash Balance" – legacy cost plus the cash balance and matching contribution benefits for future hires
  - "DC Plan" – legacy cost plus the defined contribution and matching contribution benefits for future hires

Projected Retirement Benefit Costs (except Part 2)



Projected Retirement Benefit Costs (incl. Part 2)



LTD HUMAN RESOURCES COMMITTEE
7/26/11 Page 19

Projected Costs

- The costs shown herein are for discussion purposes only, and could change significantly based upon Board action for the 2011 valuation.
  – Actuarial assumptions are generally from the 2009 valuation report.
  – For illustrative purposes, payment of the unfunded actuarial accrued liability is based upon a projected market value of assets of $11.4 million as of July 1, 2011, and 25-year level dollar payments.
  – The projections make allowance for ATU employees as of July 1, 2011 who transfer to salaried employment in future years and participate under the current benefit structure.
  – Revised assumptions for future entrants under the current plan or the cash balance plan are discussed in the slides at the end of this presentation.
  – Additional changes to assumptions used for current participants (discussed on previous slide) may increase costs further.
  – Retiree medical benefits for current employees are not included.
- Annual base salary of $5.5 million is assumed for 2011-2012, growing 3.5% per year in all future years.

Projected Costs (cont'd)

- Defined contribution costs shown above recognize that actives will have higher contribution rates in future years than they will have during the next few fiscal years.
  - To the extent that actual defined contribution costs over the next few fiscal years are lower than projected herein, the District could set aside that excess to fund the pension plan faster than it otherwise would have, or to set aside money for future years' defined contribution obligations.
- All defined benefit costs shown above are based upon meeting actuarial assumptions, and come with risks of higher contributions in the event that assumptions such as investment return are not realized.
  - Due to the lower level of benefits and more conservative assumptions, the cash balance plan entails significantly less risk than the current plan. The DC plan eliminates this risk for future entrants.

Major Decision Points

1. Adopt a new retirement benefit structure?
2. Will the new structure be cash balance or defined contribution?
    - Cost of benefits acceptable as shown?
3. Adopt a matching contribution benefit?
    - Cost of benefits acceptable as shown?
4. Current members – reduce Part 2 benefits?
    - What level of LTD-paid contributions? (0% to 6%)
    - Or change to matching contributions, same as with future hires?

Trailing Decision Points

1. Who will be covered by the new retirement benefits?
   - Date of hire on or after July 1, 2011?
   - How to handle employees who have been hired but have not commenced work?
   - Will current ATU employees who transfer into salaried positions be under the new benefits?
2. Compensation definition
   - A basic compensation definition might include regular salary, Consolidated Annual Leave used in the course of employment, and no reduction for Section 125 and 457(b) deferrals.
   - Could include OT or bonus in retirement benefits compensation, similar to OPSRP
3. Vesting provisions
   - Required minimum hours for a year of service
   - 3 to 5 years of service cliff vesting
   - Graded vesting over up to 7 years
   - Could vary vesting provisions by “main” benefit vs. matching contributions
4. Eligibility provisions
   - Length of waiting period, if any
5. Transfer provisions
   - Credit ATU service in determining accrual rate?

Trailing Decision Points

6. Retirement definition
   - Age 65 with 5 years of service
   - Age 55 with 10 years of service – would affect access to self-pay retiree medical
7. Defined contribution investments
   - Participant-directed or District-directed?
   - What investments or range of investment to use?
   - Could vary by “main” benefit and matching contribution
8. Defined contribution deposit timing
   - Payroll basis is most generous
   - Main alternative is annual deposits with end of year employment requirement
9. Matching contribution deposits
   - Payroll basis is most straight-forward and encourages ongoing participation
   - Alternatives include quarterly or annual deposits, or true-ups
   - Adopt automatic enrollment of employees?
10. Annuitization of cash balance benefit
    - Require partial or full annuitization? At what dollar levels or ages?
    - Work with a single insurer? Offer variable as well as fixed annuities?
11. Modifications to benefit formulas
    - Based on other trailing decision points, modifications to benefit formulas shown in slide 7 may be needed to meet cost goals approved by the Board as part of the Major Decision Points.

Cost Study Data

In developing the costs of current benefits and the cash balance proposal for new members, we reflected the age and gender mix of new salaried District hires from 1999-2009.

Based upon 2009 valuation data from the District, we constructed an “average” administrative new retiree as male age 62, working 2,080 hours per year and earning $65,000 in base pay. In estimating benefits under the current DB Plan, we also reflected 360 hours of cashed out Consolidated Annual Leave at retirement. For both the current and new retirement structures, overtime and bonus were included in covered compensation, but no actual amount was assumed based on the understanding that these components of compensation are not frequently paid.

Economic Actuarial Assumptions

Investment Return

The assumed investment assumption was 6.5% per year, net of investment fees, for determining the entry age normal cost for the current benefit structure and the pre-retirement defined contribution investment return. For the cash balance structure, we used an assumed investment assumption of 6.0% per year prior to retirement.

For converting cash balance and defined contribution benefits to annuities at age 62, interest rates were assumed to be 5.5% per year. This is a long-term annuity rate assumption; current rates for retirees are below 4.0%.

Salary Inflation

Salaries are assumed to increase based upon age, ranging from 11% to 7% for the employees younger than 35, down to 5.0% for employees ages 35 to 49, and 3.5% for employees age 50+. Most employees of the District are older than 35.

Cost of Living Increases

We assumed general price inflation of 2.75% per year.

Additional Actuarial Assumptions

Unless otherwise noted, actuarial assumptions were retained from the 2009 Actuarial Valuation for the current benefit structure. A detailed description of assumption changes was provided to District staff.

- RP-2000 Mortality Table for Males and Females with a 30-year projection using Scale AA. The projection of mortality is meant to reflect the new entrants whose benefits are being considered.
- Termination rates lowered for longer-service employees under the current plan in order to reflect the incentives offered by current pension and retiree medical benefits.
- Retirement rates revised for current benefits to reflect incentive for unreduced retirement at 30 years of service. Retirement rates also extended to age 67 to reflect observed experience.
- Retirement rates for cash balance proposal lowered from current levels and extended to age 70.
- All employer DC contributions (including match) will become vested.
- 80% of active members were assumed to participate and be eligible for the matching contributions up to the 3% level.

Limitations

This presentation is not intended to provide legal advice. Any legal questions resulting from this presentation should be referred to legal counsel.

Future actuarial measurements may differ significantly from the current measurements presented in this presentation due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions; changes in economic or demographic assumptions; increases or decreases expected as part of the natural operation of the methodology used for these measurements (such as the end of an amortization period or additional cost or contribution requirements based on the plan's funded status); and changes in plan provisions or applicable law. Due to the limited scope of our assignment, we did not perform an analysis of the potential range of future measurements.

111 SW Fifth Avenue
Suite 3700
Portland, OR 97204
USA

Tel +1 503 227 0634
Fax +1 503 227 7956

milliman.com

July 21, 2011

Lane Transit District
Board HR Committee

Re: Lane Transit District
New Retirement Benefits for Salaried Employees

Dear Board Members:

Following is a discussion of several decisions which should be made as part of designing the new pension retirement benefits to be implemented for LTD salaried employees hired on or after January 1, 2012.

The order of the topics generally tracks pages 20 – 22 in our June 13, 2011 presentation to the Board regarding the Retirement Program Redesign. Changes to current members' pension benefits (including Part 2 benefits) and future members' District-paid retiree medical benefits generally are not addressed in this letter.

For many of the topics, we have included specific questions, discussion points, and/or proposals. Any proposals are intended as starting points, and are not definitive recommendations.

The goal of this letter is to provide legal counsel a basis for drafting a Plan Document for Board approval. Accordingly, this letter does not address all potential administrative and consulting issues regarding the new salaried retirement benefits.

Basic Benefit Structure

On June 13, the Board instructed us to proceed on a defined contribution benefit structure with the following general format:

<u>Employer Discretionary Contribution</u>

- First five years: 4.5% of Compensation
- Years 6 – 10: 5.6% of Compensation
- Years 11 – 15: 6.7% of Compensation
- Years 16 – 20: 7.8% of Compensation
- Years 21+: 9.0% of Compensation

Employer Matching Contribution

- 50% of employee deferral on the first 6% of Compensation.

The expected long-term cost of this benefit structure is 9.2% of Compensation. However, in the first many years of implementation, the actual costs will be a lower percentage of Compensation, since most members will be receiving the lower allocation percentages on account of shorter durations of service.

The Employer Discretionary Contribution is called “discretionary” on the assumption that LTD will draft the legal documents in a way that will allow the District to change the allocation percentages in future years. This approach is designed to retain flexibility for the District, and legal counsel is exploring how best to draft the documents to retain this flexibility. The working assumption, however, is that the Discretionary Contribution will persist at its current levels indefinitely.

New Entrant Group

New salaried employees of the District hired after January 1, 2012 would participate in the new retirement benefits.

We understand that the hire date on which the employee first works an hour for the District – not the job posting date or any other consideration – would be the relevant factor in determining an employee’s eligibility for the new retirement benefits.

Should current ATU members who transfer in a future year to salaried employment be placed into the new retirement benefits?

- Legal counsel’s preliminary opinion was that future transfers to salaried employment could be placed into the new retirement benefits, and that an agreement to that effect should be signed by the employee as a condition of such transfer. This opinion is based on the assumption that no ATU employee has a right to transfer to salaried employment.
- Putting current ATU members who transfer in a future year to salaried employment into the new retirement benefits may impact the ability of the District to recruit ATU members into salaried employment, especially while the current ATU retirement benefits are in place.
- Legal counsel believes that current ATU members who transfer in a future year to salaried employment could instead be placed into the current salaried retirement benefits.

Definition of Compensation

The new retirement benefits will need to define the Compensation to which the Discretionary and Matching Contribution formulas are applied.

The current defined benefit plan definition includes salary, overtime, bonus, Extended Illness Bank (EIB) used in the course of employment, and Consolidated Annual Leave (CAL). Compensation for the current defined benefit plan is not reduced by elective contributions under IRC Section 125 and 457(a). LTD is apparently provided the flexibility to enter into individual compensation arrangements.

Following are two possible approaches to the Compensation definition:

- Base salary approach: Base salary or wages, including any employee-funded contributions to LTD's Section 125 and 457(b) plans, and CAL used in the course of employment. Overtime, bonus, cashouts of unused CAL or any other remuneration would not be included. Legal counsel recommended this option, noting that the value placed by employees on including any additional components of compensation might not be sufficient to justify the cost to LTD.

- OPSRP-style definition: Same as base salary approach above, but also including overtime and bonus.

- Legal counsel believes that the Plan document itself may not need to define Compensation. Nonetheless, the Compensation definition is an important policy decision.

Vesting Provisions

Vesting provisions determine when an employee becomes entitled to a retirement benefit. Vesting typically occurs upon reaching eligibility for retirement (discussed below) or upon attaining a length of service prior to retirement. This section addresses pre-retirement vesting provisions.

How would a Year of Vesting Service be defined?

- A Year of Vesting Service could be based upon hours worked each year, or on the elapsed time from date of hire to date of termination.

- <u>Proposal</u>: Because most LTD salaried employees work on a regular basis, an elapsed time definition seems simplest. Under this definition, the employee would earn a Year of Vesting Service on each anniversary date of the date of hire.

At what point would an employee become vested in Employer Discretionary and Matching Contributions?

- Three- and five-year cliff vesting: Upon completion of three or five Years of Vesting Service, an employee is fully vested in the retirement benefit. Leaving prior to attaining full vesting would result in complete forfeiture of all Discretionary and Matching Contributions. Cliff vesting is more prevalent with defined benefit plans.

- Graded vesting can provide a significant financial incentive to continue working with an employer throughout the vesting period, and is common with defined contribution plans, especially in the private sector. By the end of the graded vesting period, the employee's tenure is long enough that termination of employment is less likely.

- Complications can arise with graded vesting due to rehire provisions. Since the District does not engage in frequent rehiring, these complications are unlikely to be a significant source of concern.

- Longer vesting periods are allowed for public sector employees, but are probably best reserved for rich defined benefit plans.

- Vesting in defined contribution plans is very common in the event of death or own-occupation disability while employed.

- Proposal: Employ graded vesting for Discretionary and Matching Contributions. Consider seven-year grading for Discretionary Contributions to encourage retention. Consider three- to five-year grading for Matching Contributions to encourage employee deferrals as well as retention. Following is a sample vesting schedule:

Years of Vesting Service:	0	1	2	3	4	5	6	7
Discretionary Contributions:	0%	10%	20%	30%	40%	60%	80%	100%
Matching Contributions:	25%	50%	75%	100%	100%	100%	100%	100%

Entry Provisions

At what point would a new employee begin receiving Employer Discretionary and Matching Contributions?

- Under the current salaried retirement benefits, an employee participates on the January 1 or July 1 following date of hire. ATU transfers generally participate on the first of the month following transfer.

- Immediate participation is the most generous option, and is the current provision for the 457(b) plan.

- Recordkeeping considerations might provide reasons to delay entry. Delaying entry also reduces the cost of the benefits, if only slightly.

- Proposal: Consider immediate participation to begin receiving Employer Discretionary and Matching Contributions, coupled with automatic enrollment (discussed below). Alternatively, consider an entry provision of the first day of the third month following the date of hire. A common approach with this type of delayed entry provision would be to include all Compensation beginning with the first payroll on or after the entry date.

Service and Accrual Rates

The Discretionary Contributions schedule is based upon a definition of service.

- Proposal: Link up as many definitions of service as reasonably possible to avoid complications in administering and explaining the benefits. We recommend using the elapsed time Year of Vesting Service definition as the basis for other measures of service.

- Proposal: Assuming the District engages in payroll-period deposits for its Discretionary and Matching Contributions (see below), the higher accrual rates could apply beginning with the payroll next following attainment of, for example, five Years of Vesting Service.

- Proposal: ATU employees transferring to salaried employment could be credited service based upon their elapsed time employed from date of hire in an ATU position. This would mitigate the potential disincentive to transfer to salaried employment.

Definition of Retirement

Under a defined contribution benefit structure, the primary uses of retirement include full vesting of benefits and, in some cases, a requirement to distribute funds. In addition, salaried retirees are eligible for lifetime retiree medical benefits offered by and partially paid for by the District.

- Proposal: Because of the retiree medical benefits sponsored by the District, we recommend a relatively conservative definition of retirement. Following is a possible structure:

    - Normal Retirement: Later of age 65 and five Years of Vesting Service

    - Early Retirement: Either no early retirement, or later of age 55 and 15 Years of Vesting Service

    - Retiree Medical Eligibility: Eligibility for lifetime District-paid medical benefits at later of age 55, and age plus Years of Vesting Service equal or exceed 85. (Examples: age 55 and 30 Years of Vesting Service; age 65 and 20 Years of Vesting Service.) Note that for retirees who do not meet this requirement, the District will still need to make available retiree-pay-all medical coverage from Early Retirement until eligibility for Medicare.

- Proposal: We recommend that former employees also be required to receive a complete distribution of funds. Such requirement could be as soon as practicable after separation from employment, and could include an additional trigger age such as 65. This distribution requirement will reduce the District's administrative burden.

Defined Contribution Investment Options

LTD will need to choose whether to allow the participants to direct their own investments, or whether it will invest money on their behalf.

- Proposal: Allow participants to direct their own investments similar to the safe harbor provisions for participant-directed investments under ERISA law. Include in the range of available investments "target-date funds" which allocate participants' assets based upon their expected retirement date.

Selecting investment options is a complicated issue with many components. Not all components may need to be reflected in the drafting of the Plan Document. We recommend bringing in a defined contribution consultant to discuss further items such as the range of potential investments, available families of funds, and recordkeeping platforms.

Defined Contribution Deposits

Will Discretionary and Matching Contributions be deposited on a payroll-by-payroll basis, or some other periodic basis?

- Employer matching contributions are often contributed on a payroll basis. Employer discretionary contributions are sometimes made on an annual basis, and can require end-of-year employment in order to receive an allocation.

- Proposal: The simplest solution may be to make all employer and employee deposits on a payroll basis and integrate those contribution rates with payroll processing. Annual deposits of employer contributions may be difficult to integrate with the District's annual budgeting process, because end-of-year employment will not be known until after the budget has already been established.

- Assuming matching contributions are deposited on a payroll basis, we do not recommend any "true ups" of matching contributions for employees who miss deferrals for a portion of a given year.

Should employees be enrolled automatically in the 457(b) Plan?

- Employee contributions to the 457(b) Plan and the Employer Matching Contributions will be important factors for employees to amass sufficient retirement income.

- Emerging defined contribution experience indicates that many employees who might otherwise elect higher contribution percentages will instead "default" to the level set by automatic enrollment percentages.

- Proposal: Automatically enroll employees in the 457(b) plan at a level to maximize Employer Matching Contributions. Legal counsel can advise if there are any potential conflicts with this approach, but none are anticipated.

- Note the discussion below regarding the matching contribution formula. We have suggested a formula in which an employee must defer six percent of salary to obtain the maximum match.

Matching Contribution Formula

The LTD Board gave preliminary approval on June 13, 2011 to establish a Matching Contribution formula which offers contributions up to 3% of pay.

- Proposal: Set Employer Matching Contributions equal to 50% of the first six percent of Compensation deferred by employees into the 457(b) Plan. Because employee contributions to the 457(b) Plan will be an important piece in employees amassing sufficient retirement income, we recommend a Matching Contribution formula which encourages higher contribution rates.

- When reviewing potential changes to ATU benefits last year, we suggested a Matching Contribution formula of 100% of employee contributions up to 3% of Compensation. This proposal was geared towards an ATU employee group whose voluntary 457(b) deferral rates have historically been low, and whose average pay level is lower than among LTD salaried employees.

Annuitization of Benefits

One of the concerns surrounding defined contribution retirement systems is that retirees may face challenges to establishing and maintaining steady income throughout retirement. One solution to these challenges is the purchase of annuities. An annuity purchase takes a lump sum retirement account and uses it to purchase lifetime monthly income which is guaranteed by an insurance company.

- Mandates for annuity purchases are not common in employer-sponsored defined contribution retirement plans.

- Providing mandatory or optional annuity benefits through a third-party insurer would likely raise the Plan's administrative costs.

- The retirement community and Congress continue to deliberate the issues surrounding retirement income security. At this time, there is no widely adopted approach to guaranteeing retirement income from defined contribution plans which clearly recommends itself to mid-size employers. Meanwhile, it will be several years before employees begin to retire under the new retirement benefits program.

- Proposal: Do not require nor offer annuities through the LTD retirement plan. Monitor legislative and market developments.

Reliance and Limitations

Milliman's work is prepared solely for the internal business use of Lane Transit District. Milliman does not intend to benefit or create a legal duty to any third party recipient of its work product.

No third party recipient of Milliman's work product should rely upon Milliman's work product. Such recipients should engage qualified professionals for advice appropriate to their own specific needs.

The consultants who worked on this assignment are pension actuaries. Milliman's advice is not intended to be a substitute for qualified legal counsel.

We look forward to discussing these issues with the LTD Board HR Committee on July 26.

Sincerely,

Peter R. Sturdivan

Peter R. Sturdivan, FSA, EA, MAAA
Principal and Consulting Actuary

Will Cl

William H. Clark-Shim, FSA, EA, MAAA
Consulting Actuary

PRS/WHC:whc
encl.

cc: Ms. Mary Adams
Ms. Diane Hellekson
Mr. Everett Moreland