

- b) Projected salary increases of at least 4.25% per year.**
- c) An assumed annual cost-of-living adjustment that is generally 2% per annum and compounded. In addition, there is a closed group of special safety officers whose annual adjustment is equal to inflation (4.25% per year).

**Both (a) and (b) included an inflation rate of 4.25%.

The actuarial value of assets was determined using a methodology that smoothes the effects of short-term volatility in the market value of investments over a five-year period. In fiscal year 2007, the SDCERS Board approved a different asset smoothing method by marking the actuarial value of assets to market value in the fiscal year 2006 actuarial valuation, the result of which caused the UAAL to decrease by approximately \$183,800. The method used by the actuary in fiscal year 2005 was not a commonly used method. The expected actuarial value asset smoothing method commenced with the fiscal year 2007 valuation. The UAAL for funding purposes, pursuant to the Gleason Settlement, is being amortized over a fixed 30-year closed period for the fiscal years 2006, 2007, and 2008. As of June 30, 2006, the valuation year used to compute the fiscal year 2008 annually required contribution, there were 27 years remaining in the amortization period. For valuations effective June 30 2007, SDCERS' Board of Administration decided to use a 20-year closed amortization schedule with no negative amortization. Beginning with the valuation dated June 30, 2007, the normal cost and UAAL amortization cost will be determined using the Entry Age Normal actuarial method, the result of which will cause the UAAL used in the determination of the fiscal year 2009 ARC to increase by approximately \$252,200.

The following table shows the City's annual pension cost ("APC") and the percentage of APC contributed for the fiscal year ended June 30, 2008 and two preceding years (in thousands):

Fiscal Year Ended June 30	APC	Percentage Contributed	Net Pension Obligation
2006	\$ 175,879	154.28%	\$ 194,720
2007	169,762	99.63%	195,356
2008	145,077	114.82%	173,852

Net Pension Obligation

Net Pension Obligation (NPO) is the cumulative difference, since the effective date of GASB 27 (fiscal year 1998, with a 10-year look back), between the annual pension cost and the employer's contributions to the Plan. This includes the pension liability at transition (beginning pension liability) and excludes short term differences and unpaid contributions that have been converted to pension-related debt. As of June 30, 2008, the City's NPO is approximately \$173,852 and is reported in accordance with GASB 27. See table above.

The change to NPO is derived by first calculating the City's Annual Required Contribution ("ARC"). The ARC is calculated by actuarially determining the cost of pension benefits accrued during the year (normal cost) and adding to that the annual amount needed to amortize the UAAL (amortization cost) as reported by the actuary, in accordance with the amortization period and method selected. The ARC is then increased by interest accruing on any outstanding NPO (NPO Interest) and then reduced by the amortization of the UAAL that is related to the NPO (ARC Adjustment).

The following shows the calculation for NPO based on the actuarial information provided to the City (in thousands):

ARC [Fiscal Year 2008]	\$ 140,107
Interest on NPO	15,644
ARC Adjustment	(10,674)
Annual Pension Cost	<u>145,077</u>
Contributions [Fiscal Year 2008]	<u>(166,581)</u>
Change in NPO	(21,504)
NPO Beginning of Year [July 1, 2007]	195,356
NPO End of Year [June 30, 2008]	<u><u>\$ 173,852</u></u>

Components of the NPO and actions taken to address the Pension Liability

Multiple components have contributed to the City's NPO dating back to fiscal year 1988, including the use of pension assets to pay for costs related to retiree healthcare and employee contribution offset liabilities. Additionally, benefit increases resulting from the Corbett Settlement, which were initially considered contingent, were excluded from the actuarially determined ARC and the City's contributions for the fiscal years 1996-2003 were less than the ARC as a result of MP-1 and MP-2.

As part of the agreements with the labor unions, several benefits were altered or eliminated for all employees hired on or after July 1, 2005, including the Deferred Retirement Option Plan (DROP), the 13th Check, the option to purchase years of service credits ("air-time"), and retiree healthcare benefits; however, the retirement formula generally remains 2.5% at 55 for general members and 3.0% at 50 for safety members. Additionally, the City has contributed approximately \$143, 200¹ in excess of the ARC for the fiscal years 2006 through 2008.

DEFINED CONTRIBUTION PLANS

a. Supplemental Pension Savings Plan - City

Pursuant to the City's withdrawal from the Federal Social Security System effective January 8, 1982, the City established the Supplemental Pension Savings Plan ("SPSP"). Pursuant to the Federal Government's mandate of a Social Security Medicare tax for all employees not covered by Social Security hired on or after April 1, 1986, the City established the Supplemental Pension Savings Plan-Medicare ("SPSP-M"). The SPSP and SPSP-M Plans were merged into a single plan ("SPSP") on November 12, 2004 for administrative simplification, without a change in benefits. Pursuant to the requirements of the Omnibus Budget Reconciliation Act of 1990 ("OBRA-90") requiring employee coverage under a retirement system in lieu of coverage under the Federal Insurance Contributions Act ("FICA") effective July 1, 1991, the City established the Supplemental Pension Savings Plan-Hourly ("SPSP-H"). These supplemental plans are defined contribution plans administered by Wachovia Corporation to provide pension benefits for eligible employees. There are no plan members who belong to an entity other than the City. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings, less investment losses. The City's general retirement members and lifeguard members

¹ The ARCs used to calculate the additional payment of \$143,200 are actuarially determined, and therefore, do not include liabilities related to the Employee Offset Liability (fiscal years 2006 & 2007), the Corbett Settlement (fiscal years 2006 & 2007) or the Preservation of Benefits Plan (fiscal year 2008). However, the City has elected to include these liabilities in addition to the actuarially determined ARC when calculating the NPO. Liabilities excluded from the actuarial ARC but included in the City's NPO calculation amount to approximately \$11,545.