

Your Choice

Guidelines for Making the DROP Decision

For Eligible Members of the Police and Fire Retirement System of the City of Detroit

- Detroit Police Officers Association (DPOA)
- Detroit Police Lieutenants and Sergeants Association (LSA)
- Detroit Police Command Officers Association (DPCOA)
- Detroit Fire Fighters Association (DFFA)
- Non-Union Executives of the Police and Fire Departments

INTRODUCTION

The Police and Fire Retirement System of the City of Detroit (“System”) received a favorable determination letter from the Internal Revenue Service in November of 2007 for the System’s optional Deferred Retirement Option Plan (DROP) for eligible members.

System members covered by a collective bargaining agreement authorizing DROP participation are eligible to elect to participate in the DROP program if they are immediately eligible for a 25 year service retirement under the System (or such other DROP eligibility service retirement requirement as provided for in the applicable collective bargaining agreement) .

Eligible members are those that belong to the following groups:

- **Detroit Police Officers Association (DPOA)**
- **Detroit Police Lieutenants and Sergeants Association (LSA)**
- **Detroit Police Command Officers Association (DPCOA)**
- **Detroit Fire Fighters Association (DFFA)**
- **Non-Union Executives of the Police and Fire Departments**

NOTE: Once you elect to participate in the DROP Program, your election is irrevocable. You are not allowed to change or revoke your DROP election.

This booklet has been prepared to help you make your choice. Here, we will cover the following topics:

- **Understanding Your Current System Benefits**
- **Comparing the DROP Program**
- **How to Choose the Option that is Better for You**

The choice you make is completely voluntary. It is also a very personal decision. Whether remaining active in the current System or selecting the new DROP Option will be better for you will depend on your circumstances. Your choice will depend upon some or all of the following factors:

1. The relative income stream at retirement that the regular System benefit or the DROP option can be expected to produce.
2. The importance to you of characteristics such as portability, transferability, lump sum and other distribution options.
3. How long you have worked for the City and how long you intend to continue to be employed.
4. Your overall personal financial situation.

Also, this is simply a summary of DROP provisions. If there is a conflict between this document and the System’s DROP terms, or if this document is ambiguous, DROP terms govern.

PART I. UNDERSTANDING YOUR CURRENT SYSTEM PENSION

To completely evaluate your DROP option, it is important that you thoroughly understand your current System benefit. Here, we will review the basic DROP features of the System.

1. Normal Age and Service Retirement Benefit

Upon completion of 25 years of service (or such other DROP eligible years of service requirement as provided in the applicable collective bargaining agreement), you are eligible to retire. You will receive an annual pension, payable monthly, which is generally calculated as follows:

New Plan (post 1969 hires)

2.5% x years of service (up to 25) x Average Final Compensation (“AFC”), plus
2.1% x years of service (beyond 25 up to 35) x AFC

FOR EXAMPLE: If you have 25 years of service and your AFC (including longevity) is \$47,254, your benefit will be:

2.5% x 25 years = 62.5% x \$47,254 = \$29,534 annually or
\$2,461 monthly

NOTE: This is a simple example so that you have an idea of how electing to DROP actually works. Determining AFC involves a detailed calculation which is explained in the *Police and Fire Compensation Computation (AFC, FC, & Disability Maximum)* memorandum, which you can obtain from the System.

2. Average Final Compensation

AFC generally equals the average of the maximum rate of pay for your rank held in each of the last three or five years prior to retirement, depending on your retirement date and bargaining unit. See the memorandum titled “*Police and Fire Compensation Computation (AFC, FC, & Disability Maximum)*” which you can obtain from the System.

Also, in connection with your DROP election you may elect to the extent allowed pursuant to then effective bargaining agreement terms to have the applicable percentage of your eligible sick pay included for purposes of calculating your AFC (and there would be no further option available regarding use of such percentages to calculate AFC). Sick days remaining after such election, plus those additional sick days accrued while participating in the DROP as an active police officer or fire fighter with the City will be determined and paid out in accordance with your applicable collective bargaining agreement with the City.

3. Required Employee Contributions:

5% - During first 25 years of service (or such other DROP eligible years of service requirement as provided in the applicable collective bargaining agreement) only.

4. **Distribution Options:**

There are essentially three retirement options:

- (a) A defined benefit plan monthly benefit payable for the life of the participant equal to the regular age and service retirement benefit, which includes receiving defined contribution plan amounts in the form of a monthly annuity.
- (b) Actuarially equivalent Joint and Survivor Monthly Benefit Option.
- (c) Return of your employee contributions in a lump sum (known as the “Defined Contribution Plan”) which could affect your monthly benefit referenced in paragraph (a) above.

5. **Cost of Living Adjustment:**

Retirees hired before 1969 receive an increase proportionate to the annual increase received by active employees. Those hired after 1969 receive an annual cost of living adjustment of 2.25%, based upon the original retirement amount or compounded, depending on the bargaining unit.

PART II. COMPARING THE NEW DROP PROGRAM

Here is how the new Deferred Retirement Option Plan (DROP) Program works:

1. **Eligibility:**

You are eligible to irrevocably choose the DROP after you become eligible for a 25 year service retirement allowance (or other such DROP eligible service retirement requirement as provide for in the applicable collective bargaining agreement) under the System. At this point, you have essentially three choices:

- (a) Actually retire and begin receiving an immediate full monthly pension which includes defined contribution plan amounts, or take the defined contribution plan amounts in a lump sum and begin receiving a monthly pension from the defined benefit plan.
- (b) Continue working and accruing benefits under the System (based on continued service and compensation).
- (c) Continue working, but irrevocably elect the DROP Program.

2. **Choosing the DROP:**

You can choose to participate in the DROP anytime after you become eligible. It is a voluntary election. Remember, if you choose the DROP, the decision to participate in the DROP is **IRREVOCABLE**. You make your election to DROP by completing and signing the appropriate DROP election form (which you can obtain from the System) and delivering your DROP election to the System (you should also make a copy for yourself). Your DROP election date on your DROP election form must be the date you deliver the form to the System, or a future date. **Your DROP election date will be the last day you will accrue any service or compensation for computing a System pension benefit.** You cannot retroactively elect to DROP. For example, you cannot deliver a DROP election form to the System on August 1, 2009 electing to DROP on July 1, 2009.

3. Operation of the DROP:

If you choose to elect to participate in the DROP, the following will happen:

- (a) Your System benefits will become “frozen” (i.e., no further service credit or compensation will accrue).
- (b) Your contributions to the System will end.
- (c) You must choose, in writing, a form of distribution for your system pension benefit (e.g., straight life monthly benefit or joint & survivor monthly benefit) in accordance with System processes.
- (d) Effective with your DROP election, 75% of the amount of your monthly pension (including applicable escalator increases) that you would have received from the System had you actually retired on your DROP election date is instead paid into your individual DROP account where it will accrue earnings on a tax-deferred basis for as long as you participate in the DROP. NOTE: There will likely be an administrative delay before your first DROP amounts are allocated to your DROP account while the System sets up your DROP account.
- (e) At this time your DROP account will be invested in a stable value, group annuity contract product with ING that provides a credited rate of interest set once each year by ING. You should carefully review ING material detailing how your DROP account is invested. You will be provided notice of any subsequent change in the DROP investment product or provider.
- (f) Your DROP allocations will continue for as long as you continue to be actively employed as a police officer or fire fighter with the City.
- (g) While you are actively employed as a police officer or fire fighter participating in the DROP, to the System’s knowledge you are subject to the same employment rules and regulations as before you elected to participate in the DROP. You will continue to be paid your wages as an employee. To the System’s knowledge, your seniority status will not be affected during your DROP participation. However, you will not accrue any additional credit towards retirement as a DROP participant.

Participation in the DROP does not guarantee continued employment.

- (h) When you end your active employment as a police officer or fire fighter with the City you may take a distribution from your DROP account or you may directly roll over your DROP to an IRA.
- (i) At the end of your DROP Participation, when you retire, you will begin to receive 100% of your “frozen” System pension (including annual escalator amounts) that you would have received had you initially retired at the date you elected to participate in the DROP, plus you will be entitled to the value of your individual DROP account (which, together, are subject to applicable IRS limits on “annualized” benefits. The IRS limit on annual benefits is \$195,000 in 2009. Your DROP benefit is annualized to apply the limit).

PART III. HOW TO CHOOSE THE OPTION THAT IS BETTER FOR YOU

This is an important choice. In order to make an informed and comfortable decision, you should take the following steps:

STEP ONE: Acquire as Much Knowledge as Possible.

Learn all you can about the operation and characteristics of the System and the DROP option. In addition to this booklet, some other tools that will help you are:

- **Annual Report of the Retirement System and your collective bargain agreement.**
- **Attending a Scheduled Group Informational Meeting with representatives from ING.**
- **Review ING investment materials.**
- **Consulting with your DROP Plan Retirement Plan Specialist and/or Personal Financial Adviser.**

STEP TWO: Obtain Benefit Projections from Each Option.

The income that each option can be expected to produce is, for most people, one of the most important factors in making their decision.

Note: Any results from such analysis are simply projections and are highly dependent upon the salary increase and earnings rate assumptions that are used. They do not constitute any promise or guarantee of benefits that will eventually be obtained from either the System pension and/or DROP.

STEP THREE: Do Some Comprehensive Retirement Planning.

No doubt the income stream from the retirement option that you select will be a major source of support for you and your family after you cease active employment with the City. However, it will not be the sole and exclusive means to provide you with retirement income. To develop a comprehensive forecast of your retirement income situation you need to consider some or all of these other sources:

- **Social Security Benefits**
- **Any 457 Deferred Compensation Plan you may have**
- **IRAs and Personal Savings (including amounts rolled over from the defined contribution part of the pension plan)**
- **Spouse's Retirement Plans**
- **Wages from Part Time Employment**
- **Other Sources of Income**

You should also do a personal inventory as well, considering additional factors, which may affect the type of retirement option you should choose:

- **How long you intend to be employed with the City**
- **Your health, that of your spouse and family health and longevity history**

- **The ages and support needs of your children or other dependents**
- **Whether you would want to leave any remaining retirement assets to heirs after you die**
- **The particular lifestyle you wish to live after full-time employment**

CONCLUSION

Your System provides you (and your spouse, if elected) with a guaranteed income stream for life after you retire.

In the DROP, you may have a lower pension as compared to if you continued in the System, but you will accumulate an account (the DROP account) that can also provide an income stream or a lump sum. A DROP account will offer you portability and investment reward/risk.

The option which is better for you is a matter of individual choice based upon your particular personal and family situation. If you follow the steps mentioned above, we believe you can make the choice that is right for you.

APPENDIX A

FREQUENTLY ASKED QUESTIONS ABOUT THE DROP

1. What is the Deferred Retirement Option Plan (“DROP”)?

The DROP is a voluntary election by you to freeze your System pension benefit at the time of your DROP election, and to have an amount equal to System pension otherwise payable to you, as if you had then retired, instead allocated to a separate DROP Account earning interest until you actually retire. At retirement you are entitled to your frozen System pension as of your DROP election and your DROP account balance.

2. Who is eligible to participate in the DROP?

Eligible members are System members in the following groups:

- **Detroit Police Officers Association (DPOA)**
- **Detroit Police Lieutenants and Sergeants Association (LSA)**
- **Detroit Police Command Officers Association (DPCOA)**
- **Detroit Fire Fighters Association (DFFA)**
- **Non-Union Executives of the Police and Fire Departments**

and who are immediately eligible for a 25 year service retirement (or such other DROP eligible service retirement requirement as provided in the applicable collective bargaining agreement).

3. When will participation in the DROP begin?

If you are otherwise eligible, you may now begin to make DROP elections.

4. Is there a minimum or a maximum period that I must stay in the DROP?

No. However, you will remain in the DROP as long as your employment as a police officer or fire fighter with the City continues. You may choose to actually retire anytime after entering the DROP. Then you will then begin receiving your frozen pension amount plus whatever amounts have accumulated in your individual DROP account.

5. What happens if I die or become disabled during the DROP Program?

If you die while in the DROP and before termination of employment as a police officer or fire fighter with the City, your System benefit will revert to your regular, pre-DROP “frozen pension”, plus applicable adjustments, and it will be payable in accordance with your System benefit election on file and which was made in connection with your DROP election. Your named beneficiary, or if none then your estate, will be entitled to the amounts remaining in your DROP account.

If you become disabled while an employee in the DROP and your employment as an active police officer or firefighter with the City is terminated because you are disabled, you shall immediately be retired and commence the form of System retirement selected at DROP commencement plus applicable pension improvement increases. You are also entitled to your DROP account. You will not be entitled to disability retirement benefits.

6. If I elect the DROP, does my employment status change?

If you elect the DROP, to the System's knowledge, you will have the same rights and privileges as other active employees of the City. However, you will accrue no additional System defined benefit pension plan and defined contribution plan benefits, and you will have DROP allocations made to your DROP account.

7. What happens with my sick pay if I elect the DROP?

If you elect the DROP, the System understand that the City's position is that you have two choices regarding your sick pay, as follows:

- You can cash out 100% or 85% (as applicable) of your sick pay at the time you elect the DROP. Your sick pay will be paid to you within the time required by your collective bargaining agreement in accordance with your rate of pay in effect at the time you elect the DROP. From your DROP election forward you will accumulate additional sick days as an employee. Any sick pay you accrued while participating in the DROP and which remains at termination of your employment will be paid to you after your termination based on your rate at termination; or
- You can, coincident with your DROP election, elect to have the applicable percentage of your sick pay pursuant to your collective bargaining agreement (e.g., 25%) used in the computation of AFC for pension (and DROP) purposes. 100% or 85%, as applicable, of any unused sick pay as of your DROP election can either:
 - be paid to you, within the time required by your collective bargaining agreement, after you DROP based on your pay rate in effect at the time you elected the DROP; or
 - remain in your sick bank for payment when you terminate, provided payment of that sick pay is based on your compensation in effect when you elected the DROP.
NOTE: Your Union's position is that the balance of your unpaid sick pay is payable at the rate in effect when you terminate employment.

After you elect the DROP, you will accrue additional sick days while employed and participating in the DROP. When you terminate, those "post-DROP" sick days accumulated while you participated in the DROP will be paid out based on your compensation rate in effect when you terminate employment.

8. If there are increases to the System's benefit formula made while I am in the DROP Program, will they apply to my frozen benefit?

No, unless the benefits are specifically made retroactive to cover prior years of service before your DROP election.

9. If I am promoted while I am participating in the DROP, will my System pension change when I retire?

No. Upon your DROP election your System pension freezes and will not change (except for applicable escalators).

10. How may I take distributions from my DROP account?

You can take distributions in any form that you wish as long as it is permitted by the IRS. You can withdraw all your amounts in a lump sum (which may be rolled over to an IRA), take periodic distributions, purchase an annuity or any combination of the above. You may also refrain from taking immediate distributions and leave your account to accumulate until you are required to take distributions at age 70-1/2. Again, you may rollover all or a part of your DROP account into an IRA or a qualified plan that accepts such rollovers.

11. What are the tax consequences of taking distributions from my DROP account?

Basically, DROP account distributions are subject to income tax when withdrawn unless rolled over to an IRA or another employer's plan. Additionally, there is a 10% penalty on distributions, or withdrawals taken before age 59-1/2 (unless rolled over). However, there are many exceptions to this rule. There is no penalty if:

- You separate from service (i.e., retire), and are age 55;
- You are any age and take withdrawals "on a periodic basis over your life, or joint life, expectancy" (like an annuity).
- If you die, become disabled, or have a severe medical necessity for yourself or your dependents.

12. Will my DROP account run out of money if I live longer than my life expectancy?

Theoretically, this is possible. It should be noted that your DROP account is only one source of income that you are likely to have at retirement. Your defined benefit plan, Social Security, deferred compensation through any 457 Plan, IRAs, personal savings and perhaps even wages are other possible sources.

The longevity risk can be managed in at least two ways:

- By taking slightly smaller monthly withdrawals designed to last longer than your normal life expectancy; and
- By purchasing a guaranteed life annuity with a portion of your DROP balance.

13. Is there a guarantee that my DROP account will never decrease?

The DROP is currently investing in a stable value group annuity contract with ING providing an annual credited rate which can not be less than zero. Also, at distribution the DROP provides for a distribution of at least your DROP allocations.

14. Am I able to take a loan from my DROP account?

No.

15. What if I am in the process of getting divorced, or I get divorced in the future ?

DROP assets, like other forms of pension benefits, may be considered marital property subject to division in a divorce proceeding. While DROP assets are not subject to distribution until a

member terminates active employment as a police officer or fire fighter with the City, pursuant to a domestic relations order a court can award all or part of your DROP account to a former spouse in the same manner as it can assign other retirement payments to a former spouse.

16. What if I am divorced, there is a domestic relations order in effect, and I want to elect to DROP?

If you are eligible to make a DROP election, you are divorced, and your System pension is subject to a domestic relations order currently in effect, you are strongly advised to review the specific terms of the domestic relations order that is in effect. You may also want to seek assistance from your attorney. With respect to those DROP eligible members whose benefits are subject to a domestic relations order, if they elect to DROP the System plans to review such orders on a case by case basis to determine if the order affects the amount of their DROP election or assigns all or part of their DROP account.

17. Can I withdraw my defined contribution plan contributions in a lump sum, and still participate in the DROP program?

Yes.

18. Can I find out more about how the DROP is invested?

ING Life Insurance and Annuity Company, the designated administrator and investment provider for the DROP Plan will conduct thorough group and individual education sessions concerning all aspects of the DROP investment vehicle.

The decision is left to you whether to DROP. **You are urged to also consult with your personal financial advisor.**

19. How can I get more information?

Entering the DROP is a big decision. Once a decision is made to enter and approved, it is FINAL. Before entering the DROP you are encouraged to contact your Union representative with your questions about DROP procedures. If you have questions about your DROP account and how it is invested, contact: Mark J. Woolhiser of ING at (734) 207-8800. The DROP is a valuable benefit, but like anything, it does not meet everyone's needs in the same way. Before you elect to participate in the DROP, be sure of your rights and make careful plans for your future. It would be wise to consult with your own financial adviser concerning the choices that are most advantageous for your specific circumstances.