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March 7, 2017

Mr. David B. Clark
Executive Director
Arkansas Local Police and Fire Retirement System
620 W. 3rd, Suite 200
Little Rock, Arkansas 72201-2212

Re: Senate Bill 222

Dear Mr. Clark:

You have asked us for our analysis of Senate Bill (SB) 222 as it relates to the Arkansas Local Police and Fire Retirement System (LOPFI). SB 222 modifies Arkansas State Code Title 24, Chapter 10, Subchapter 7 concerning participation in the Local Police and Fire Deferred Retirement Option Plan (DROP). In particular, SB 222 adds a new section which allows a member to defer receiving payment of the participant's DROP account one time. The member may leave the funds in the plan and receive interest at a rate of 2% per year. The funds must be distributed to the member no later than upon the attainment of age 70 ½ years.

We anticipate that no increase in employer contributions would result due to adoption of the proposed legislation. No explicit modeling of the proposed legislation was performed. The analysis instead considered the makeup of the current active population, as reported in the valuation data and LOPFI DROP experience to date. A participant would presumably leave the funds in the plan if the 2% interest credit was perceived as being more valuable than receiving a distribution or DROP annuity benefit immediately.

Based on projected future DROP activity, DROP balances left with LOPFI after retirement could be $30-50 million (in current dollars). We expect such usage only in very low interest rate environments (such as the last decade). The expected effect on LOPFI is as follows:

- Generally, very little and not negative, as we do not expect low interest rates to be the normal state.
- Possibly negative in a low interest rate environment and if annual LOPFI investment returns are less than 2%. It appears unlikely that LOPFI would have been negatively impacted if the proposed provision had been in place in the past decade.
- LOPFI may be negatively impacted if there is any impairment to the investment program from keeping up to 3% of assets in cash (to meet potential immediate cash outs by members leaving DROP balances on deposit).

Please review this letter carefully to ensure that we have understood the bill properly. The analysis in this letter should not be relied upon if there is doubt about our understanding of the bill. Our analysis relates only to the plan changes described in this correspondence. In the event that other plan changes are being considered, it is very important to remember that the results of separate

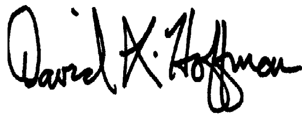
actuarial analyses cannot generally be added together to produce a total. The total can be considerably greater than the sum of the parts due to the interaction of various plan provisions with each other, and with the assumptions that must be used.

We did not review this bill for compliance with Federal, State, or local laws or regulations, and internal revenue code provisions nor did we attempt to determine whether these changes would contradict or negate other related State, or local laws or provisions of other proposed legislation. Such a review was not within the scope of our assignment.

Heidi G. Barry is a Member of the American Academy of Actuaries (MAAA) and meets the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

This communication shall not be construed to provide tax advice, legal advice or investment advice.

Respectfully submitted,



David L. Hoffman

Heidi G. Barry, ASA, MAAA

DLH/HGB:mrb