Original Article

A tale of the prichard (AL) pension program

Received (in revised form): 16th January 2012

Semoon Chang

is a Professor of Economics and a Director of the Center for Business & Economic Research at the University of South Alabama. He has served as a President of the National Association for University Business & Economic Research and the Homeless Coalition of Mobile. He is a panelist of the CESifo World Economic Survey. His recent articles appeared in *Quarterly Journal of Labor Policy*, *International Journal of Mass Emergencies and Disasters*, and *Oil, Gas, & Energy Quarterly*.

ABSTRACT On 22 December 2010, *The New York Times* reported that ‘Prichard did something that pension experts say they have never seen before: it stopped sending monthly pension checks to its 150 retired workers’. Prichard is a small city in southwest Alabama. Thirty-five per cent of Prichard residents live below the poverty level, and 85 per cent are African-Americans. This article introduces the progression of the Prichard pension from its inception to the unprecedented temporary halt in payment and then resumption of payment in reduced amount.

Pensions (2012) 17, 112–120. doi:10.1057/pm.2012.11

Keywords: municipal pension; pension default; prichard (AL); public pension; failed pension

INTRODUCTION

Public sector pension funds with excessive liabilities have been well documented. For instance, ‘Pension plans operated by state governments on behalf of their employees are underfunded by an estimated \$452 billion according to official reports, with total liabilities of \$2.8 trillion and total assets of \$2.3 trillion in 2008. However, many economists argue that even these daunting liabilities are understated. Using methods that are required for private sector pensions, which value pension liabilities according to likelihood of payment rather than the return expected on pension assets, total liabilities amount to \$5.2 trillion and the unfunded liability rises to \$3 trillion’. (p. 1)¹

Mitchell states that ‘The current economic environment has produced a “perfect storm” for public pensions, where low interest rates are spiking liabilities, depressed equity markets are

whittling away assets, and economic recession is drying up state and local tax revenue. ... Inasmuch as public employee pensions are not guaranteed by the federal government, it is even possible that public sector plans might default. Whereas this has not happened to date in the United States, it is true that a few cities and towns (including Cleveland, OH, and Bridgeport, CT, as well as Vallejo, CA) have declared bankruptcy’. (p. 12)²

The dubious honor of being the first city in the nation to default on pension obligations goes to Prichard, which is located in Mobile County, Alabama. Interestingly, ‘The first recorded default by a local government unit [also] occurred in Mobile, Alabama in 1938’. (p. 9)³ On 22 December 2010, *The New York Times* reported that ‘Prichard did something that pension experts say they have never seen before: it stopped sending monthly pension checks to its 150 retired workers, breaking a state law requiring it to pay its promised retirement benefits in full’, and that ‘So the declining, little-known city of Prichard is now attracting the attention of bankruptcy

Correspondence: Semoon Chang
Department of Economics, University of South Alabama, Mobile,
Alabama 36688, USA

lawyers, labor leaders, municipal credit analysts and local officials from across the country. They want to see if the situation in Prichard, like the continuing bankruptcy of Vallejo, Calif., ultimately creates a legal precedent on whether distressed cities can legally cut or reduce their pensions, and if so, how'.⁴ 'The situation in Prichard is extremely unusual in that a public pension plan has actually defaulted'.⁵

The Prichard pension dilemma has also been reported in the Huffington Post on 23 December 2010, and by the Canadian Broadcasting Company on 26 January 2011. 'Prichard's problems have triggered national concern for the fate of municipal pension funds across the country – both the *Wall Street Journal* and *The New York Times* have published articles highlighting Prichard's troubles, and CBS News has attended at least one of the city's council meetings. "There is a precedent being set here", Coale said. "The whole country is watching, and they will find that they can take from retirees and no one will stop them"'.⁶

After reviewing eight centuries of world history on defaults of government debt, Reinhart and Rogoff concluded that 'The lesson of history, then, is that even as institutions and policy makers improve, there will always be a temptation to stretch the limits. Just as an individual can go bankrupt no matter how much she starts out, a financial system can collapse under the pressure of greed, politics, and profits no matter how well regulated it seems to be'.⁷ Financial system in this quotation may be replaced by pension programs of local government employees, and short-sightedness may be added to the list of pressure in the quotation. This article introduces the story of the Prichard pension problem.

PRICHARD (ALABAMA)

Prichard began as a settlement in the 1830s and was incorporated in 1925 as a city in Mobile County, Alabama. During World War II, Prichard, the then city of the predominantly White race, became prosperous when many shipbuilding companies and paper companies adjacent to the city's boundary led to

construction of homes for their workers in the city. In 1960, Prichard recorded a population of 47371. Following the civil rights movement in the 1960s, however, many African-Americans began to move into the heart of Prichard and a White flight soon followed.

In 1972, while still a majority White city, Prichard elected its first Black mayor, Algernon Johnson (A.J.) Cooper, who served two terms, and then served in the administration of President Bill Clinton. During the 1980s and 1990s, two major employers adjacent to Prichard, Scott Paper and International Paper, closed their doors, and the city's financial base took a direct hit. Prichard filed for bankruptcy in 1999 and again in 2009. The official Website of Prichard lists the city's median family income at US\$23519. Thirty-five per cent of the residents over 25 years of age failed to complete high school, and only 7 per cent, compared with 19 per cent for the state of Alabama, earned a bachelor's degree or higher. Thirty-five per cent of Prichard residents live below the poverty level as compared with 16 per cent for the state of Alabama. The population of Prichard steadily declined to 27576 in 2009 of which 85 per cent were African-Americans.

PRICHARD PENSION PLAN

The pension plan for retirees of the city of Prichard was established in 1956 by a special Act of the Alabama Legislature that applied only to Prichard. The 1956 pension plan was amended by the Legislature more than 15 times, increasing the city's mandatory contribution from 5 per cent to the current 10.5 per cent, although employees' contribution has remained at 5.5 per cent.

Importantly, a 1963 amendment of the city's Pension Act required the city to pay the losses, if the pension board makes mistakes in granting pension benefits, or if the bank invests unwisely or if the stock market collapses.⁸ 'The benefits provided for the employees of the City of Prichard hereunder shall not be reduced or prorated among those properly entitled thereto and should, at any time, the fund be insufficient to pay in full the benefits and to defray the expenses provided for, it shall be the duty of the governing body of the City of Prichard,

Alabama, to make provision therefore in accordance with the provisions hereof'.⁹

Obviously, 'It is not just the pensioners who suffer when a pension fund runs dry. If a city tried to follow the law and pay its pensioners with money from its annual operating budget, it would probably have to adopt large tax increases, or make huge service cuts, to come up with the money. Current city workers could find themselves paying into a pension plan that will not be there for their own retirements. In Prichard, some older workers have delayed retiring, since they cannot afford to give up their paychecks if no pension checks will follow'.⁵

In 1975, control of the pension plan was taken away by the state legislature from the city and given to the new Pension Board to oversee retirement benefits. The Pension Board 'shall consist of four members to be selected by the city council of the City of Prichard and three members elected by the employees of the city'.¹⁰ Mayor of Prichard has no control over selection of the members of the Pension Board.

In 1983, 'Refunds of employee contributions to non-vested employees changed from 50 per cent to 100 per cent'. (p. 37)¹¹ In addition, in 1983, 'pensioners were to get increases at 50 per cent of the rate employees received each year, with no increase in contributions'. (p. 37)¹¹ In 1991, 'employees with 25 or more years now could receive 100 per cent in benefits at age 55. Previously, if less than age 60, benefits would have been reduced just like Social Security. This change had a significant negative impact on the plan, but yet there was no offsetting increase in contributions'. (p. 34)¹¹ According to the current bylaw, an employee may retire after a minimum of 20 years of work to qualify for an annual pension at 50 per cent of the average 'compensation' over the last 4 calendar years. Pension payment begins at the age of 55 and the percentage of 50 increases to 60 per cent as the year of services increases to 30 years.¹²

'No one knows or acknowledges when the practice began, but at some point the Pension Board, without legislative approval and contrary to provisions passed in 1975, began adding the accumulated unused sick, vacation and

compensatory (SVC) hours (times the current rate of pay) to the pension calculation. The effect of this one change was to increase pension benefits by an estimated average of 26 per cent, with no offsetting contribution or revenue source to pay for it'. (p. 38)¹¹ 'The fund's rules say that the final benefit was to be calculated according to the average of the worker's last four years on the job. But instead of simply tallying the last 4 years, the city clerks who executed the fund also included a lump-sum payment for the worker's unused vacation, sick and compensatory time'.⁸ Some workers had thousands of hours of time saved up over their careers, meaning that lump-sum payments of these workers were easily a year's pay.⁸

'The pension plan itself does not explicitly say that the lump-sum payment should be included in the calculation. It only says that the pension calculation should be based on a percentage of the employee's 'salary or other compensation'. That's the way the calculation was done since at least 1975, according to Mary Berg, who worked in Prichard's city clerk's office'.⁸ 'Nate Doss, a district chief with the Prichard Fire Department who still works for the city, said that during the late 1980s and early 1990s, the city actively encouraged employees to think of the pension as a way to make up for low pay. The city had no money to award overtime or make more hires, he said, thus officials encouraged public-safety employees to bank compensatory time and vacation time, promising that it would help them when they retired. The unabated accrual of comp and vacation time may have prevented a worker exodus, but it transferred a substantial portion of the cost of paying employees from the general fund to the pension fund'.⁸

'As evidence of his good faith when he took office in 2004, [Mayor] Davis points to a blue-ribbon committee that he set up to investigate the pension and try to find a way to salvage it. By the time the committee issued its findings in 2006, the pension was underfunded by \$20 million'.⁸ Further, Prichard was not able to add any additional money to make up for the roughly \$100 000 per month in negative cash flow carried by the pension fund, because the city revenues,

Table 1: General fund revenues and pension fund balances

<i>FY</i>	<i>Taxes</i>	<i>Licenses and permits</i>	<i>Inter-governmental</i>	<i>Fines and costs</i>	<i>Miscellaneous</i>	<i>Total</i>	<i>Value of pension fund</i>
2000–2001	5317600	3241300	0	442066	778245	9779211	8279710
2002	4819451	3282683	22062	333862	686878	9144936	7149400
2003	4778817	3550834	90221	217292	896407	9533571	6771992
2004	4792400	3256621	143753	196762	403442	8792978	6148499
2005	5631891	3391717	160731	256320	352300	9792959	5573651
2006	6137842	3768349	298683	253761	488867	10947502	4662730
2007	5778563	2559766	48007	221082	2243851	10851269	3658768
2008	5846202	2533706	774173	244949	2082603	11481633	1698727
2009	5523781	2573092	1280589	274456	1910679	11562597	26809
2010	5143223	2310971	853580	220670	1713309	10241753	651372

Notes: (a) Miscellaneous from 2008 to 2010 may not correspond to Miscellaneous for previous years.

(b) Pension fund balances are for the end of September of each year.

Source: Annual audit reports.

especially from taxes and licenses/permits, had been shrinking for many years. The general funds of Prichard since fiscal year 2002 are summarized in Table 1.

Pension payments to all retirees stopped after the payment in September 2009 when the entire balance of the pension fund reached no more than \$26 908 as shown in Table 1. Partial payments, about a third of the obligated amount, were resumed in June 2011 as explained later in this article. Even without proration, ‘By the standard of other public pension plans, and the six-figure pensions that draw outrage in places like California and New Jersey, it is not especially rich. Its biggest pension came to about \$39 000 a year, for a retired fire chief with many years of service. The average retiree got around \$12 000 a year’.⁵

It may be noted that most state and local government pension plans in Alabama are covered by the Retirement Systems of Alabama (RSA), which is widely believed to have been well managed. ‘But at least 10 [public sector] pension plans [in Alabama] are run by a city or county, or other small independent group’.¹³ Prichard pension plan is one of the 10 or so that are not a member of the RSA. When Prichard asked to join the RSA, the RSA officials required \$16.5 million of pre-payment as a condition to accept the Prichard pension plan. In addition, the Prichard pension plan is not covered by the insurance program of the Pension Benefit Guaranty Corporation, created by the Employee Retirement Income Security Act of 1974

(ERISA), which protects pension benefits in private-sector traditional pension plans known as defined benefit plans.

IMPACT OF THE FALLING STOCK PRICES DURING 2007–2009

The City of Prichard annual financial reports as summarized in Table 1 indicate that as of the end of September, each year, the pension funds balance had been: \$8 279 710 in 2001; \$7 149 400 in 2002; \$6 771 992 in 2003; \$6 148 499 in 2004; \$5 573 651 in 2005; \$4 662 730 in 2006; \$3 658 768 in 2007; \$1 698 727 in 2008; \$26 809 in 2009; and \$651 372 in 2010. The declining balances before the 2007 financial crisis clearly indicate that the main problem is more excessive pension benefits than fallen stock prices, although taking funds out of the stock market in January 2009 when stock prices were low did not help. The Prichard pension fund balance was \$4 416 601.47 in January 2007. In January 2009, pension funds were pulled out of the stock market. In September 2009, pension payments stopped when the balance was only \$26 808.96 well below about \$150 000 needed to pay the retirees each month. The balance in January 2011 increased to \$838 545.83, aided in part by additional contributions made by the City. The trend of the Prichard pension fund balances from January 2007 to September 2010 is summarized in Table 2. A partial pension payment was resumed in June 2011.

In Table 2, Column (2) is the difference between revenues to the pension fund and

Table 2: Prichard pension funds balances

<i>Month/Year</i>	<i>Revenues – payments</i>	<i>Begin balance + (2)</i>	<i>(3) + Yields from T-notes</i>	<i>Actual balance on book</i>	<i>Losses and gains (5) – (4)</i>	<i>DJ industrial</i>
<i>(1)</i>	<i>(2)</i>	<i>(3)</i>	<i>(4)</i>	<i>(5)</i>	<i>(6)</i>	<i>(7)</i>
Begin balance		4 506 942.53				
January 2007	(140 819.68)	4 366 122.85	4 383 441.80	4 416 601.47	33 159.67	12 313
February 2007	(116 546.27)	4 249 576.58	4 266 291.58	4 288 531.37	22 239.79	12 078.9
March 2007	(120 486.10)	4 129 090.48	4 144 781.02	4 201 001.44	56 220.42	11 926.8
April 2007	(118 691.12)	4 010 399.36	4 026 073.34	4 187 214.29	161 140.95	12 284.5
May 2007	(79 504.86)	3 930 894.50	3 946 454.29	4 186 129.02	239 674.73	12 993
June 2007	(110 176.22)	3 820 718.28	3 836 956.33	4 043 427.48	206 471.15	13 205.1
July 2007	(123 600.30)	3 697 117.98	3 712 522.64	3 850 997.52	138 474.88	13 143.9
August 2007	(149 419.49)	3 547 698.49	3 561 504.95	3 729 035.87	167 530.92	12 455.9
September 2007	(157 740.59)	3 389 957.90	3 402 726.74	3 658 768.31	256 041.57	12 992
October 2007	(97 054.59)	3 292 903.31	3 305 334.02	3 611 516.00	306 181.98	13 337.9
November 2007	(95 248.24)	3 197 655.07	3 208 713.63	3 432 677.79	223 964.16	12 707.3
December 2007	(120 906.72)	3 076 748.35	3 087 260.57	3 309 623.68	222 363.11	13 059.3
January 2008	(140 633.83)	2 936 114.52	2 945 265.41	3 054 000.79	108 735.38	11 508.7
February 2008	(124 374.22)	2 811 740.30	2 820 503.56	2 855 449.01	34 945.45	12 006.8
March 2008	(120 228.52)	2 691 511.78	2 699 384.45	2 710 367.13	10 982.68	11 650.4
April 2008	(114 605.73)	2 576 906.05	2 584 808.56	2 666 889.95	82 081.39	12 208.4
May 2008	(121 163.83)	2 455 742.22	2 463 682.45	2 571 600.52	107 918.07	12 397.6
June 2008	(129 100.23)	2 326 641.99	2 334 591.35	2 228 805.21	(105 786.14)	11 226.3
July 2008	(115 548.07)	2 211 093.92	2 218 482.66	2 083 111.73	(135 370.93)	10 732
August 2008	(136 340.94)	2 074 752.98	2 081 478.64	1 955 533.05	(122 945.59)	11 144.6
September 2008	(109 379.80)	1 965 373.18	1 971 416.70	1 698 726.70	(272 690.00)	10 266.8
October 2008	(102 314.50)	1 863 058.68	1 868 973.89	1 365 630.95	(503 342.94)	7 773.71
November 2008	(139 609.42)	1 723 449.26	1 728 519.07	1 144 629.54	(583 889.53)	7 392.27
December 2008	(106 723.42)	1 616 725.84	1 619 986.24	1 063 670.37	(556 315.87)	8 072.47
January 2009	(103 565.71)	1 513 160.13	1 516 337.77	925 169.82	(591 167.95)	7 856.86
February 2009	(117 466.41)	1 395 693.72	1 399 031.75	765 216.13	(633 815.62)	6 952.06
March 2009	(81 425.42)	1 314 268.30	1 317 356.83	716 077.72	(601 279.11)	6 440.08
April 2009	(181 935.43)	1 132 332.87	1 135 097.65	541 781.26	(593 316.39)	7 450.74
May 2009	(159 153.43)	973 179.44	975 847.57	383 053.09	(592 794.48)	8 047.54
June 2009	(110 153.05)	863 026.39	865 701.77	272 976.20	(592 725.57)	8 236.07
July 2009	(75 231.79)	787 794.60	790 131.72	197 779.65	(592 352.07)	8 057.57
August 2009	(39 223.54)	748 571.06	750 810.54	158 559.58	(592 250.96)	9 078.28
September 2009	(131 752.39)	616 818.67	618 566.32	26 808.96	(591 757.36)	9 223.08
October 2009	29 377.17	646 195.84	648 021.34	56 186.71	(591 834.63)	9 378.77
November 2009	46 350.63	692 546.47	694 508.68	102 538.05	(591 970.63)	9 647.06
December 2009	45 775.77	738 322.24	740 531.05	148 314.90	(592 216.15)	10 207.3
January 2010	47 143.61	785 465.85	787 907.34	195 460.02	(592 447.32)	10 014.4
February 2010	70 408.64	855 874.49	858 506.30	265 870.54	(592 635.76)	9 822.84
March 2010	67 671.47	923 545.96	926 416.65	333 544.52	(592 872.13)	10 320.1
April 2010	83 551.75	1 007 097.71	1 010 328.82	417 099.28	(593 229.54)	10 810.2
May 2010	43 860.75	1 050 958.46	1 053 953.69	460 963.70	(592 989.99)	9 756.11
June 2010	41 590.07	1 092 548.53	1 095 461.99	502 557.73	(592 904.26)	9 726.33
July 2010	43 114.49	1 135 663.02	1 138 511.64	545 676.28	(592 835.36)	9 596.04
August 2010	61 850.31	1 197 513.33	1 200 207.73	607 560.89	(592 646.84)	9 915.73
September 2010	43 734.63	1 241 247.96	1 243 989.05	651 371.69	(592 617.36)	10 016
October 2010	40 926.16	1 282 174.12	1 284 888.06	692 356.56	(592 531.50)	10 682.7
November 2010	41 120.70	1 323 294.82	1 326 338.40	733 538.03	(592 800.37)	10 906.5
December 2010	42 146.87	1 365 441.69	1 369 185.28	775 750.91	(593 434.37)	11 007.3
January 2011	62 736.55	1 428 178.24	1 432 212.84	838 545.83	(593 667.01)	11 577.4

payments out of the pension fund. Revenues are comprised of monthly contributions by the city, contributions by employees and others such as occasional additional contributions by the city. Payments are benefits paid to retirees and administrative expenses. Figures in the parentheses refer to payments that are greater than revenues.

Note that the balance turned positive only after payments stopped beginning in October 2009. Figures in Column (3) are the beginning balances on accounting ledger at the end of 2006 to which figures in Column (2) are added. Figures in Column (3) show the trend in fund balances in the absence of any income or loss from

investments. Column (4) figures are Column (3) figures adjusted for the assumption that the monthly balances are invested in 10-year Treasury notes at the interest or yield prevailing during the same month. Figures in Column (5) are the actual pension fund balances at the end of each month that are maintained by the Pension Board. Figures in Column (5) include income from investments, capital gains and capital losses. Figures in Column (6) are figures in Column (5) from which figures in Column (4) are subtracted. Put differently, figures in Column (6) represent the difference between balances invested in safe Treasury notes and balances invested in the stock market during January 2007 and December 2008. Column (6) figures thus represent economic losses (or gains in the parentheses) from investing in the stock market. Column (7) figures are the low Dow-Jones Industrial stock price indices for the month.

A simple regression of the Losses and Gains in Column (6) as a function of stock prices for January 2007 to December 2008 indicates the extent of the impact of falling stock prices on the balance of the Prichard pension funds. Note that funds were taken out of the stock market in January 2009. The figure in the parentheses below the estimated coefficient is the standard error of the estimated coefficient. The *t*-value is 21.8580, while the 95 per cent confidence intervals of the estimated coefficient are 132.9418 and 160.8131.

$$\text{Loss} = -1702752 + 146.8774\text{DJ}(6.7196)$$

$$R^2 = 0.96$$

$$D - W = 1.54$$

The loss of Prichard pension funds from the falling stock prices can be estimated by multiplying \$146.8774 to the difference in Dow Jones index between January 2007 and December 2008, which is 4240.53 (= 12313 – 8072.47). The loss thus estimated is \$622838.02. This loss is slightly higher than the ‘loss in investment’ showing in the books of the Pension Board for the same period, which is \$553055.47. This is probably because the loss in this article includes what the fund balances could have earned if they were invested in 10-year Treasury notes during

the same period at the rates that prevailed in each of the 24 months. Needless to say, the loss could have been recovered somewhat if the shrinking fund balances were kept in the stock market beyond December 2008. The amount that could have been recovered is not expected to be large, however, because the fund balances were shrinking rapidly.

LEGAL PROCEEDINGS

The burden of pension payments led Prichard to file bankruptcy on 5 October 1999, and another one on 27 October 2009. The city, not the Pension Board, filed these bankruptcies because the Prichard pension program made the city responsible for any shortfalls in pension funds, not the Pension Board as a separate entity.

The Plan of Readjustment of Debts for the City of Prichard for the 1999 bankruptcy was filed on 30 June 2000 and was approved on 16 July 2000. The Order confirming the readjustment of debts by the US Bankruptcy judge was issued on 6 October 2000. Key adjustments included in the Order were: ‘The City shall continue to pay its ten and one-half per cent (10.5 per cent) contribution to the Pension Plan’; ‘All existing and future pension benefit payments will be reduced by eight and one-half per cent (8.5 per cent), except for those retirees receiving less than \$500.00 monthly, or surviving spouses’; ‘There will be no further pension increases for retirees based upon wage increases for employees’; and ‘Pension Plan assets will continue to be invested in equity securities, except for an amount equal to that to be paid to retirees over the subsequent nine (9) months, which will be invested in fixed income securities’. Although none of the national media paid attention at that time, what was considered unthinkable in the public sector pension programs, that is, a cut in pension benefits, did happen in 2000.

Only 2 years after the city paid off its creditors from the 1999 bankruptcy, the City of Prichard again filed for bankruptcy on 27 October 2009 in an attempt to cope with the debt and lawsuits relating to the pension payments. According to Mayor Ron Davis, ‘Over the past 50 years, the pension plan was amended by the Legislature

more than fifteen times, and always the economic burden on the City was increased'. It should be noted that the city filed the 2009 bankruptcy because the city was not able to pay for the shortfalls in the pension obligation, not because the city was unable to meet daily financial obligations.

The Plan of Adjustment for the 2009 bankruptcy was filed on 19 May 2010. Amendments to the Plan were filed on 27 May, 3 August and 30 August, all during 2010. Amended Disclosure Statement was also filed on 30 August 2010. Key plans and adjustments were: 'After the Effective Date, the City will continue to set aside 10.5 per cent of each payroll. Under the current budget this is approximately \$27500.00 a month. Also, there are approximately 157 retirees participating as vested pensioners under the existing pension plan. For a period of ten (10) years, the City will pay to each claimant in this class their pension obligation up to a maximum of \$200.00 per month per claim. Currently, certain retirees' monthly pension payment is for less than \$200.00/month. For these retirees, the Plan provides for a full payment of the monthly obligation during the period for which retiree payments are made under the Plan'.¹⁴ And 'As of 30 June 2010, there was \$502557.73 in the dedicated pension fund. These funds represent monies paid in by both current employees and by the City. Of the monies in the dedicated fund, \$155061.16 are the monies that have been withheld from the wages of the City's existing employees since the filing of the petition. Under the terms of the Plan, such funds, withheld from current employees, will be placed in a separate account for the benefit of the City's current employees and the City's obligations to provide retirement benefits to those employees'.¹⁵

On 31 August 2010, US Bankruptcy Judge William Shulman dismissed Prichard's bankruptcy case, stating that the city was not eligible for Chapter 9 under Alabama Law. The city had filed for bankruptcy in October 2009, a month after retirees stopped receiving pension checks. In a plan to emerge from bankruptcy, the city had offered to pay pensioners \$190000 to be divided

among retirees, and then give each retiree \$200 a month for 10 years. A group of retirees had sued the city, but that case was put on hold, along with all other civil suits against the city, during the bankruptcy proceedings. Stewart said he believed those civil cases would now be able to move forward.

Following the 31 August ruling by Judge Shulman, Prichard retirees filed a lawsuit against the city on 1 September 2010. Pensioners had filed suit earlier in 2009, asking city officials to ensure that the fund was solvent, but that case was put on hold when Prichard filed for bankruptcy in October 2009. The lawsuit filed on 1 September 2010 alleges that the city filed for bankruptcy a day before attorneys planned to depose Mayor Ron Davis.

In January 2011, 'Mayor Davis has proposed that the Prichard water and sewer board stop billing the city about \$25000 a month for fire hydrant service. In turn, beginning next year the city would take that amount off the franchise fee the water board pays the city in January. Of the \$25000 per month, the mayor said, \$15000 would go into the pension fund so the city could begin making partial payments to retirees, who have received no money since September 2009. Under his plan, the other \$10000 would defray the cost of general city operations'.¹⁶ Early in February 2011, Mayor Davis made another proposal of reduced pensions. Full payment without adjustment was \$153221.59 per month during 2011, although the proposed adjustment would have lowered the payment to \$38305.40. The proposal was not accepted.

On 12 May 2011, the Prichard City Council rejected another proposal by the city to make partial payments. According to the proposal, the city will make one-time payment of \$650000 from about \$1 million currently in the pension fund to the attorney for the retirees to share, and make monthly payments equal to about one-third (that is, total about \$50000 per month) of what the retirees are supposed to receive. After a 13 May 2011 meeting of lawyers for the city and the retirees in the Mobile County Circuit Court that has to approve the agreement, the City Council scheduled another meeting on 19 May

to discuss the city's proposal that the City Council rejected on 12 May. On 19 May 2011, the Prichard City Council approved the proposed agreement after making an amendment on the agreement that made the city and its insurance company, not the retirees, to be responsible for payment to the bankruptcy attorneys if the city pursued bankruptcy again. On 25 May 2011, Mobile County Circuit Court Judge Michael Youngpeter approved the 19 May agreement.

19 MAY 2011 AGREEMENT

The 19 May Agreement is 16-pages long, written in single-space full of strange terminologies and statements, including 'any person who would otherwise be considered a Retiree except for his or her death shall not be considered to be a Retiree after the date of said death'. There are two key components in the Agreement: 'Monthly Payment' and 'Betterment Distribution Payments'.

The monthly payment is the share among individual retirees of the \$50 000 that the city is making available each month. The payment formula is:

$$\text{IAMA} = \$50\,000 \times (\text{IROMA} / \text{TROMA})$$

In which "IAMA" is the Individual Adjusted Monthly Amount, which is the amount payable to the Individual Retiree for the particular month, "IROMA" is the Individual Retiree's Original Monthly Amount and "TROMA" is the Total Retiree's Original Monthly Amount, which is the total of all then remaining Retirees' Original Monthly Amounts'. (p. 9) For instance, if retiree A were originally receiving \$1000 per month and the total of all original payments to all retirees were \$150 000 per month, the Agreement allows retiree A to receive:

$$\$50\,000 \times (\$1000 / \$150\,000) = \$333.33$$

The better distribution payment is the one-time payment of about \$500 000 that all retirees share based on the formula:

$$\text{CP} = \text{BD} \times (\text{IRAA} / \text{TRAA})$$

in which 'ICP' is the amount payable to the the Individual Retiree, (BD) is the total Betterment Distribution being disbursed, (IRAA) is the Individual Retiree's Remaining Arrearage Amount and (TRAA) is the total amount of all remaining Retirees' Remaining Arrearage Amount'. (pp. 9–10) For example, if retiree A's arrearage amount is \$20 000 and the total arrearage amount of all retirees is \$2 750 000, retiree A's share is:

$$\$500\,000 \times (\$20\,000 / \$2\,750\,000) = \$3636.36$$

The better distribution amount may be repeated during a fiscal year in which the city's revenues exceed an amount calculated based on a formula in the Agreement. The Agreement led to the resumption of a partial payment in June 2011.

US District Court Judge Kristi Dubose in Mobile asked the Alabama Supreme Court during the week of 15 May 2011 to determine whether Prichard has the right under state law to seek Chapter 9 bankruptcy protection over pension funds. The request by Judge Dubose for clarification by the Alabama Supreme Court relates to the city's appeal of the 2010 ruling by US Bankruptcy Judge William Shulman to dismiss the city's bankruptcy petition. Judge Shulman's ruling allowed retirees to resume their lawsuit against the city over the city's failure to make pension payments in full. 'Meanwhile, the bankruptcy remains dismissed and the appeal will be on hold'.¹⁷

The 19 May 2011 deal that allowed the partial payment from June 2011 did not mention current employees. Recognizing the needs of a clearer pension structure for current employees, Mayor Davis made a proposal in September 2011 in which 'current employees who are old enough and have the requisite years of service would be able to retire with about a third of their expected benefits', and 'the best that the younger employees could hope for under the proposal would be to see their own contributions thus far returned to them in full, plus 25 per cent' that they can 'put into a 457 plan, which is the

government equivalent of a 401(k) plan'.¹⁸ For the agreement to take effect, a 50 per cent of the current employees would have to sign it. They have yet to vote on the proposal, however. All are 'waiting for the Alabama Supreme Court to rule on whether a city with no bond debt can use bankruptcy protection to restructure other liabilities, such as its pension obligation'.¹⁸

EPILOGUE

The 10 June 2011, 20:00 Hannity Show on Fox News commented that the Prichard pension problem was the fault of 'politicians'. Reality is not that simple. The leading politician of all in the city's pension problems is the city's mayor. However, the mayor may be legally responsible for the shortfalls of the pension funds, but the mayor's only choice was to make partial payments, or un-incorporate the city. Mayor has no control over the pension board, and has to manage a shrinking city with declining revenues. Real causes of the Prichard pension problems are many and include, but are not limited to, state constitution that does not allow home rule, past members of the pension board who pushed for increased pay without an increase in contributions, state legislatures that allowed changes in calculation methods that led to higher pension benefits, and the predominantly poor African-American composition of the city's race mix that led to a benign neglect for all the city's past and current problems by leaders at all levels of the government in which Prichard is located.

When this author volunteered without pay to review the city's pension fund problems early in 2011, this author asked Mayor Davis a question: After all the nationwide publicity of the city's pension fund problems, did anyone from the state legislature, the Mobile County Commission, the Alabama Governor's Office or the federal government offer an assistance? Mayor responded: 'No, except you'.

REFERENCES AND NOTES

- 1 Norcross, E. and Biggs, A. (2010) The Crisis in Public Sector Pension Plans: A Blueprint for Reform in New Jersey. Working paper of the Mercatus Center at George Mason University no. 10-31, June.
- 2 Mitchell, O.S. (2009) The future of public employee retirement systems. In: O.S. Mitchell and G. Anderson (eds.) *The Future of Public Employee Retirement Systems*. New York: Oxford University Press Inc., pp. 1-15.
- 3 Advisory Commission on Intergovernmental Relations. (1973) *City Financial Emergencies: The Intergovernmental Dimension*. Washington: ACIR, July, p. 12.
- 4 Cooper, M. and Walsh, M.W. (2010) Alabama town's failed pension is a warning. *The New York Times* 22 December.
- 5 Haller, M. (2010) Alabama town's failed pension is a warning. *The New York Times* 22 December.
- 6 Kramer, J. (2011) Remembrances: Residents gather at service, recalling losses. *Press-Register* 11 March: 1C and 6C, quotation from p. 6C.
- 7 Reinhart, C.M. and Rogoff, K.S. (2009) *This Time is Different: Eight Centuries of Financial Folly*. Princeton, NJ: Princeton University Press, pp. 291-292.
- 8 McClendon, R. (2011) What busted Prichard pension. *Press-Register* 29 May: p. 4.
- 9 Baylaw Section XV. Liability of City, p. 10.
- 10 Baylaw Section XVIII. Board of Pensions, p. 11.
- 11 Reibling, M.C., Jackson, L.A. and Hunter, S. (2006) Survival Project for the Municipal Employees Pension and Relief Fund. Report prepared by consultants for the City of Prichard, 11 January.
- 12 Baylaw Section XI. Retirement Benefits - 20 Years of Service, pp. 5-7.
- 13 Faulk, K. (2011) Future shock for some public pension plans. *Press-Register* 29 May: 13C.
- 14 3 August 2010 Second Amended Plan of Adjustment, p. 9.
- 15 30 August 2010 Third Amended Disclosure Statement of City of Prichard, p. 9.
- 16 Editorial. (2011) At least Prichard is trying to help retirees. *Press-Register* 23 January.
- 17 Kramer, J. (2011) Prichard pension deal is passed. *Press-Register* 20 May: 4A.
- 18 McClendon, R. (2011) Mayor moving to close pension. *Mobile Press-Register* 25 September: 4A.

FURTHER READING

- City of Prichard. (2011) Agreement between certain retirees and the city of Prichard, Alabama. 19 May.
- City of Prichard, Annual Financial Statements, 2007-2010.
- City of Prichard Bylaw. (2002) Municipal Employees Pension and Relief Fund (Provisions Effective as of 1 January).
- U.S. Bankruptcy Court for the Southern District of Alabama. (2010) Chapter 9 Proceedings for Prichard, Case no.: 09-15000, 'Plan of Adjustment' 19 May; 'First Amended Plan of Adjustment' 27 May; 'Second Amended Plan of Adjustment' 3 August; and 'Third Amended Plan of Adjustment' 30 August; 'Third Amended Disclosure Statement of City of Prichard' 30 August.