City of San Antonio

Agenda Memorandum

File Number:15-1431

Agenda Item Number: 5.

Agenda Date: 2/12/2015

In Control: City Council A Session

DEPARTMENT: Finance

DEPARTMENT HEAD: Troy Elliott

COUNCIL DISTRICTS IMPACTED: Citywide

SUBJECT:

Amendment to City's State 84th Legislative Session Program that the City does not support any legislation for the San Antonio Fire and Police Pension Fund ("Fund") which would increase benefits and/or increase the unfunded liability of the Fund.

SUMMARY:

On September 24, 2014, the Board of Trustees of the San Antonio Fire and Police Pension Fund ("Fund") approved proposed amendments to the State Statute that governs the Fund. These amendments include an increase in retirement benefits for active uniform fire and police employees, an increase in the cost of living adjustment for certain retirees, delegation of authority to the Board of Trustees to approve future cost of living enhancements for certain retirees, and a reduction in the City's annual contribution to the Fund. Based on an analysis done by the Fund's actuary from the October 1, 2013 actuarial study, these changes would increase the unfunded liability of the Fund by $72.6 million or 31.2% and extend the projected time to pay off the unfunded liability of the Fund from 7.25 years to 12.87 years. The reduction in the City's annual contribution to the Fund is estimated at approximately $4.3 million.

City Staff reviewed the proposed legislative amendments and recommended to the City's Intergovernmental Relations (IGR) Committee on October 8, 2014 and on November 12, 2014 to not support the proposed legislative amendments. On November 12th, the IGR Committee approved the following language as part of the upcoming State Legislative Program "That the City does not support legislation that increases benefits and/or increases the unfunded liability of the San Antonio Fire and Police Pension Fund". The language was approved by the IGR Committee by a three-to-one vote, with one absentee.

At the request of the Mayor on December 1, 2014, independent firms were engaged to review the proposed changes to the Pension Fund. Gabriel, Roeder, Smith & Company (GRS) was engaged to conduct the actuarial review and Coastal Securities, one of the City's co-financial advisors was engaged to review the impact on the City's 'AAA' general obligation bond rating. GRS noted that the Fund is in a strong financial position due to the financial commitment from the City as well as effective management from the Fund's Board and staff. In order to maintain or improve the strong position of the Fund, GRS also noted that the City should develop a written funding, or "road map" that clearly defines the City's contribution commitment to the Fund and the potential for future benefits modifications. Coastal Securities concluded that the adoption of the proposed changes to the Fund may result in the downgrade of the City's 'AAA' general obligation bond rating by one or more of the major bond rating agencies.

BACKGROUND INFORMATION:

The Fund is a statutory trust providing a defined benefit plan for retired police officers and fire fighters (and their beneficiaries), and disability and death benefits for current police officers and fire fighters (and their beneficiaries) employed by the City of San Antonio. It is governed by Article 6243o of Vernon's Texas Civil Statutes (the "Act"). The members of the Fund contribute 12.32% of their total salary to the Fund and the City of San Antonio double matches this amount at 24.64% of total salary. For fiscal year 2015, the City is projected to contribute approximately $76 million to the Fund.

Last year, the Board of Trustees of the Fund requested suggestions from the City for their review and consideration in preparing for the 2015 Legislative Session. In response and consistent with the recommendation of the City Council appointed Health Care & Retirement Benefits Task Force (also known as the "Legacy Task Force"), the City provided suggestions to the Fund to include evaluation of a defined contribution plan, introduction of a new tier with lower benefits, and to modify existing benefits, in order to reduce contribution levels or become fully funded. The Fund rejected the City's suggestions and refused to study the impact of any of these suggested changes.

Rather, on September 24, 2014, the Fund Board of Trustees approved a legislative package to include the following proposed changes to benefits, governance and contributions in the pension fund statute:

<u>Benefit Changes</u>

- Extends the 100% of CPI cost-of-living adjustment (COLA) to all members who retired between October 1, 1999 and September 30, 2003 (currently, all members that retired after October 1, 1999 receive a COLA of 75% of CPI);
- Reduces the formula for a Disability Pension Benefit form 50% of Average salary to 47.5% of average salary;
- Changes the maximum service allowed for BackDROP from 34 years to 33 years; and,
- Increases the benefit formula to the following percentages:

Service Years	**Benefit % Of Current Plan**	**Cumulative % Of Current Plan**	**Benefit % Of Proposed Plan**	**Cumulative % of Proposed Plan**
1-20	2.250%	20 years = 45.00%	2.375%	20 years = 47.50%
21-27	5.000%	27 years = 80.00%	5.000%	27 years = 82.50%
28	2.000%	28 years = 82.00%	2.500%	28 years = 85.00%
29	2.000%	29 years = 84.00%	0.500%	29 years = 85.50%
30	2.000%	30 years = 86.00%	0.500%	30 years = 86.00%
31-33	0.500%	33 years = 87.50%	0.500%	33 years = 87.50%

Governance Change
Gives the Board discretion regarding adjusting the retirement date applicable to the determination of whether a retired member receives a 75% of CPI COLA or a 100% of CPI COLA, subject to safeguards determined by the Fund.

Contribution Change
Reduces the City's contribution rate from 24.64% of payroll to 23.25% and the member rate of 12.32% of payroll remains unchanged, which results in a reduction of approximately $4.3 million to the City's current annual contribution of $76 million.

The Fund's actuary, Segal Consulting, evaluated the impact of the Fund's proposed legislative package and determined that the package would increase the unfunded liability (UAAL) by $73 million; increase the normal cost rate by 0.85% of payroll (or $2.6 million in the first year); and increase the funding period (or years to eliminate the unfunded liability) by 5.62 years. These changes would be an increase to the current UAAL of $209,951,480 and the amortization period (or years to pay off the unfunded liability) of 6.15 years as of the October 1, 2014 actuarial valuation.

City Staff reviewed the proposed legislative amendments and recommended to the City's Intergovernmental Relations (IGR) Committee on October 8, 2014 and on November 12, 2014 to not support the proposed legislative amendments. On November 12th, the IGR Committee approved the following language as part of the upcoming State Legislative Program "That the City does not support legislation that increases benefits and/or increases the unfunded liability of the San Antonio Fire and Police Pension Fund". The language was approved by the IGR Committee by a three-to-one vote, with one absentee.

At the request of the Mayor on December 1, 2014, independent firms were engaged to review the proposed changes to the Pension Fund. Gabriel Roeder Smith & Company (GRS) was retained to analyze the amendment proposal from an actuarial perspective and to evaluate whether the legislative amendment proposal is within the range of accepted best practices for pension fund management.

GRS indicated that the Fund is in a strong financial position due to the continued financial contribution to the Fund by the City, as well as effective management by the Fund. However, GRS concluded that, to maintain or improve the strong financial position, the City and the Fund need to "lay out a road map" or written funding policy that clearly communicates the City's contribution commitment and potential for future benefit modifications. Current best practices from actuaries, governmental associations, and others encourage public retirement systems and their sponsors to adopt such a written funding policy. GRS also indicated that the lowering of the City's contributions assist with short-term budgeting, but delay full funding for an additional 5.62 years at an extended cost of $172.1 million as shown in the table below. This projection does not take into consideration the growth in payroll and the resulting increase in contribution amount by the City over this period of time.

	Years 1-7	**Years 8-13**	**Total**
Current	$38.0	$0.0	$266.0
Proposed Leg Package	$33.7	$33.7	$438.1
Difference	*$(4.3)*	*$33.7*	*$172.1*

Coastal Securities was also retained to review the underlying general obligation bond ratings of the City of San Antonio and assess the potential impact of the Fund's proposed legislative package on the City's "AAA" credit rating assigned by the three major rating agencies, Moody's Investors Service, Fitch, and Standard & Poors, respectively. Coastal analyzed the impact of the proposed legislative changes to the Fund through the context of the existing ratings reports. Coastal concluded that given the current negative outlook assigned by Moody's already represents challenges to the City, even before the proposed legislative changes are considered; and that given the current rating environment, the adoption of the Fund's proposed legislative changes may result in the downgrade of the City's 'AAA' general obligation bond rating by one or more of the rating agencies.

ISSUE:

Whether to amend the City's 84th State Legislative Program to include a recitation regarding the San Antonio Fire and Police Pension Fund.

ALTERNATIVES:

The City could support the amendments to the Fund proposed by its Board of Trustees which could potentially result in a downgrade of the City's 'AAA' general obligation bond rating. Additionally, as noted above, the City would forgo the opportunity to have the Fund become fully funded in the near future as well as have a comprehensive discussion regarding a funding policy and a potential significant reduction in the City's contribution to the Fund in the near term. As noted above, approximately $38 million of the City's total $76 million contribution is allocated to paying off the unfunded liability of the Fund.

FISCAL IMPACT:

If the changes proposed by the Board of Trustees of the Fund are not supported, there is no financial impact and contributions and retirement benefits would remain the same. If the changes proposed by the Fund are adopted during the Legislative Session it will increase by about 5.62 years the time required to pay off the unfunded liability of the Fund. It is projected to require an additional $172.1 million in contributions from the City to eliminate the unfunded liability of the Fund. With passage of the legislation, the City's contribution would be reduced $4.3 million annually.

RECOMMENDATION:

Staff recommends that the City include in its 84th Legislative Session program that it not support any legislation that increases benefits and/or increases the unfunded liability of the San Antonio Fire and Police Pension Fund. The City and the Fund should capitalize on the opportunity to develop a "Funding Policy" that focuses on becoming fully funded and defining the City's contribution commitment to the Fund and the potential for future benefit modifications. This type of funding policy would be consistent with the policies and practices the City has instituted which support the City's excellent 'AAA' general obligation bond rating.