

PRB Draft Legislative Recommendations
Funding Policy and Funding Soundness Restoration Plan

Funding policy and FSRP requirements are currently separate and do not tie together to form a continuum of funding support to plans and sponsors. The funding policy requirement, enacted in 2019, requires plans to adopt a funding policy targeting full funding. The FSRP statute, enacted in 2015, requires plans and their sponsors to adopt a remediation plan if the unfunded liability cannot be amortized over 40 or fewer years.

Now that plans have funding policies, they have long-term plans to achieve full funding. However, the remediation plan requirement for plans that face serious funding shortfalls operates independently of the newer funding policy mandate and does not require plans to target full funding over a closed period in line with *PRB Funding Guidelines*.

Ideally, funding policies and funding restoration plans should work together to provide a clear path toward full funding (funding policy), and when negative experience impedes funding progress, provide a mechanism to get back on track (restoration plan). To provide an effective continuum of funding support for Texas pension plans, the FSRP, which is designed to quickly shore up dramatic funding problems, should tie back to the funding policy, which is designed to prevent funding deficiencies.

The Actuarial Committee is recommending the following for Board approval, incorporating comments and input from public retirement systems, their consultants, and other stakeholders, to improve current funding policy and funding soundness restoration plan statutory requirements.

Potential Change to Funding Policy Requirements

- 1. Sponsor involvement.** Add the sponsor to the funding policy requirement so that both the pension board and plan sponsor have ownership in the plan to achieve full funding rather than only in the remediation plan once funding problems require immediate action. Specifically, require the plan and sponsor to jointly develop the funding policy.

Potential Changes to FSRP Requirements

- 2. Increase sponsor accountability and tie funding policy and FSRP together**

Funding policy revision. Incorporate the funding policy upon trigger of FSRP. If an FSRP were triggered, the plan and sponsor would be required to adopt an FSRP and revise the funding policy together to ensure both parties are involved in long-term improvement. For FSRP plans, the revised funding policy should include a detailed plan to share the cost of unexpected actuarial losses that could derail progress toward the FSRP goal.

Sponsor adoption. Require the sponsor's governing body (e.g., city council) to adopt the FSRP through resolution to ensure full sponsor involvement and ownership.

3. Update threshold, target and trigger

Lower threshold and target to 30 years. Bring the FSRP threshold and target in line with *PRB Guidelines* and other standard-setting bodies by changing 40 years to 30 years (*PRB Guidelines* upper bound).

Tiered trigger and phase in of lower threshold. (Effective 9/1/2025) Trigger the FSRP requirement immediately for:

- a. plans that receive an AV with the amortization period **over 40 years**; and
- b. plans that receive an AV with an amortization period **between 30 - 40 years and a funded ratio lower than 65%**.

For plans that receive an AV with an amortization period **between 30 - 40 years and a funded ratio of 65% or above**, the FSRP is triggered after three consecutive annual AVs, or two consecutive AVs if the systems conduct the valuations every two or three years. 30-year amortization period target would not be expected to be achieved until 9/1/2025.

Credit for reforms already made. Plans (and sponsors) that receive an AV with an amortization period between 30 – 40 years should not become subject to the FSRP requirement if they are receiving contributions on an actuarially determined basis, even if they do not receive the full ADC each year, and the AV indicates they are on a path towards full funding.

4. Update timelines and consequences if original FSRP is not working

Timeframe for developing FSRP. Allow **one year**, rather than 6 months, for the completion of the FSRP, but also require a progress update at 6 months which should include a draft plan or changes under consideration.

OR

Allow **2 years**, rather than 6 months, for the completion of the FSRP, but also require progress updates at 1 year and at 18 months. Progress updates should include a draft plan or changes under consideration.

Future actions. Clarify that FSRPs may not include items requiring future action such as votes of the membership and that the FSRP must memorialize actions taken. FSRPs may include contribution schedules for future increases.

Shorter implementation timeframe. Remove 10-year period to reach target and require plans to achieve 30 years or less no later than 2 years from the triggering valuation.

Failure to achieve FSRP goal. If a plan and sponsor become subject to a second FSRP within a period of 10 years from adoption of the first FSRP, the second FSRP and revised funding policy shall include stricter requirements for funding restoration, such as:

- a. risk-sharing mechanisms;
- b. an ADC-based contribution structure;
- c. adjustable benefit or contribution mechanisms;
- d. a lower amortization period target: 10-25 years (per the *PRB Funding Guidelines*)

5. Update required documentation

- Require FSRPs to provide an aggregate analysis of multiple changes specifically showing how the combined impact of the changes in the FSRP would result in meeting the statutory requirements. The analysis must include an actuarial projection that shows the unfunded liability decreasing to zero within the required time period. The plan and sponsor should share the cost of the analysis.
- Clarify that any assumptions must be made in accordance with ASOPs.