PROPOSED PENSION REFORMS

AUSTIN FIREFIGHTERS RETIREMENT FUND

SEPTEMBER 2024

DRAFT

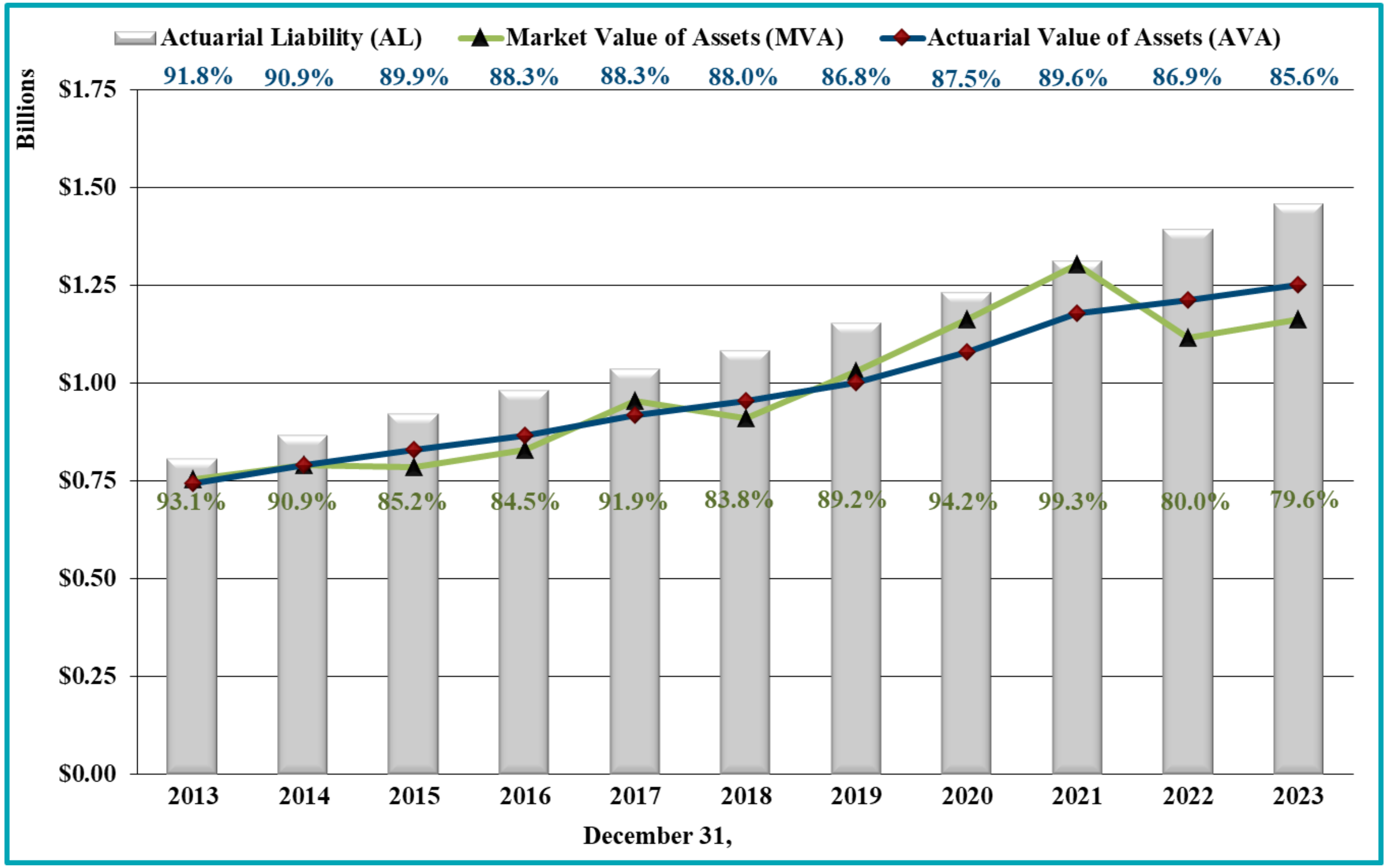
FUND STATISTICS

As of 2023 Actuarial Valuation

Actuarial Accrued Liabilities
$1.65 Billion
Market Value of Assets
$1.16 Billion
Funded Ratio
85.6%
Amortization Period
48.6 years
Investment Return Assumption
7.30%
Actual Investment Return (2023)
8.4%
Membership
2241 Members (1246 active, 995 annuitants)

FUND HISTORY

Funded Ratio



PROCESS AND CURRENT STATUS

- Fund Board established a Working Group to look at potential pension reform
- Working Group established goals for the reforms
- Began communications with the City of Austin and the membership, including its Retirement Plan Committee
- Developed these proposed benefit reforms considering such communications and working with the Fund actuary and attorney
- These proposals are in *draft form only and are simply an update*
  - Have NOT been formally adopted by the Board
  - Have NOT been agreed to by the City of Austin

PRINCIPLES OF BENEFIT REFORMS

- To ensure the Fund has sufficient assets in the long-term to preserve the ability to pay promised benefits.
- To ensure the Fund delivers an adequate level of benefits to our members
- To address the funding structure to better match Fund liabilities
- To provide a more predictable COLA that can be adequately pre-funded
- To provide members financial flexibility to structure their retirement income
  - Allow members to choose the DROP vs guaranteed COLA
- To incorporate transition measures in order to prevent adverse effects relating to proposed changes
  - Accelerated DROP withdrawals or "rush to retirement"
- To take action now to save costs

CURRENT RETIREES

- Modify the existing COLA Structure
  - **Current**: Annual, 100% CPI COLA subject to financial stability test
  - **Proposed**: Guaranteed, deferred 1% COLA
- Retain ability to participate in both DROP and COLA, but not at the same time
- Keep the current level of DROP interest rate, except for periods of negative return

CURRENT RETIREES

Modified COLA Structure

- **Members <u>without</u> DROP Accounts at 1/1/2026:**
  - Members will be eligible for 1% Automatic COLA starting the January 1st after the later of *<u>age 62 or 5 years after retirement.</u>*

- **Members <u>with</u> DROP Accounts at 1/1/2026:**
  - Members will be eligible for a 1% Automatic COLA starting January 1 following one year after the DROP balance has been completely withdrawn, but no earlier than *<u>age 67 or 5 years after retirement</u>*.
    - **Note**: Members may choose to keep the balance of DROP Accounts in the Fund past age 67. The 1% Auto COLA would start January 1 following one year after DROP balance is completely withdrawn.

CURRENT RETIREES

DROP Interest Rates

- Fund market return exceeds 0.0% for the calendar year:
  5.0% (same as now)

- Fund market return at or less than 0.0% for the calendar year:
  2.5%

- May choose to keep the balance of DROP Accounts in the Fund until April 1st of the year after the year in which the member attains age 70 ½ (same as now).

  - The 1% Auto COLA would start 1 year after DROP balance is completely withdrawn.

CURRENT ACTIVES

- Modify the existing COLA Structure
  - **Current**: Annual, 100% CPI COLA subject to financial stability test
  - **Proposed**: Guaranteed, deferred 1% COLA at later of age 62 or 5 years
- Members must choose to participate in DROP or receive a COLA
  - Members do not have opportunity for both at the same time
  - Exception for Grandfathered Actives who are currently eligible for normal retirement
- Keep the current level of DROP interest rate, except for periods of negative return (same as retirees)

CURRENT ACTIVES

Modifications to COLA Structure

- **Non-DROP Retirees**: 1% Auto COLA at the later of age 62 or 5 years after retirement.
- **DROP Retirees**: no eligibility for the 1% Auto COLA except for certain members who are grandfathered.

CURRENT ACTIVES

DROP Interest Rates

(Same as Retirees)

- **Pre-retirement**: DROP accumulation period interest rate is 5.0%
- **Post-retirement:**
  - Fund market return exceeds 0.0% for the calendar year: **5.0%** (same as now)
  - Fund market return at or less than 0.0% for the calendar year: **2.5%**
- Current Actives who retire with a DROP balance choose to be DROP participants---no COLA available <u>except for</u> certain members who are grandfathered.

GRANDFATHERED ACTIVE MEMBERS

- Active members who are eligible for normal retirement on or before 1/1/2026 are "grandfathered"

- COLA eligibility for grandfathered members who retire with DROP Accounts at or after 1/1/2026:
  - Members would have to choose after retirement and before age 62 to either:
    - Continue participating in DROP, earning interest on their DROP account beyond age 62, or
    - Participate in the 1% automatic COLA that would start the later of age 67 or 5 years after retirement

  - If choose to continue with the DROP, no eligibility for the 1% Auto COLA.
    - DROP Interest is the same as Retirees (5% or 2.5% if negative calendar year return)
    - May choose to keep the balance of DROP Accounts in the Fund until April 1 of the year after the year in which the member attains age 70 ½ (same as now)

  - If choose to participate in the COLA, members would have to take a full DROP distribution by age 62.
    - If a member withdraws their entire DROP before age 62, the 1% Auto COLA would start at the later of age 67 or 5 years after retirement

NEW HIRES

*Hired after 1/1/2026

- Multiplier lowered from 3.3% to 3.0%
- Retro-DROP feature removed (Forward DROP only)
- DROP interest rate <u>*reduced*</u> to 4% or 2% if negative calendar year return
- Contribution Rate <u>*reduced*</u> from 18.7% to 17.0%
- Normal form of retirement benefit changed to Single Life Annuity (changed from Joint and 75% Survivor annuity)
- No interest credited on returned contributions for non-vested members
- DROP or deferred COLA chosen at retirement, but not both

NEW HIRES

Modified COLA Structure

- **Non-DROP Retirees**: 1% Auto COLA at the later of age 62 or 5 years after retirement.
- **DROP Retirees**: no eligibility for the 1% Auto COLA

NEW HIRES

DROP Interest Rates

- **Pre-retirement**
  - DROP accumulation period interest rate is 4.0%
- **Post-retirement:**
  - Fund market return exceeds 0.0% for the calendar year: **4.0%**
  - Fund market return at or less than 0.0% for the calendar year: **2.0%**
- Those new hires who retire with a DROP balance choose to be DROP participants - no COLA available.

NEW HIRES

Plan Features	Current	Proposed Legislative Changes
Multiplier	3.30%	**3.00%**
Avg. Salary Length	36 months	No change
Normal Retirement Eligibility	Age 50 with 10 years of service or 25 years of service at any age	No change
Early Retirement (ER) Eligibility	Age 45 with 10 years of service or 20 years of service at any age	**No early retirement offered**
Retro-DROP	Up to 7 years, DROP account includes benefits and member contributions accumulated with 5%	**No Retro-DROP offered**
Forward DROP	Up to 7 years, DROP account includes benefits and member contributions accumulated with 5%	**Same as current except DROP account balances accrue interest at 4% during accumulation, upon retirement the DROP balances accrue interest at 4% if the Fund earns over 0% and 2% if the Fund earns at or below 0%**
Member contribution rate (New Hire)	18.7%	**17.0%**
Payment Form	Joint and 75% Survivor	**Single Life Annuity**
Non-vested terminations	Receive contributions with 5% interest credited	**Receive contributions with 0% credited interest**
COLA	COLA based on CPI-U paid from NR eligibility, subject to fiscal sustainability	**At retirement, must choose either:** **1. DROP (No COLA)** **2. NR with 1% Deferred COLA (No DROP)**

ILLUSTRATED COSTS – CURRENT MEMBERS

$ in Millions **Results Illustrated as of December 31, 2023**	**Current Design**		**Pension Reform Proposal**
COLA Assumption	2% Immediate	0% Immediate	1% Deferred
Actuarial Liability (AL)			
Actives	$677.0	$583.5	$597.6
Inactives, not including DROP balances	883.2	729.8	781.7
DROP Balances	147.2	147.2	152.8
Total Actuarial Liability	$1,707.4	$1,460.6	$1,532.0
Actuarial Value of Assets (AVA)	1,162.7	1,162.7	1,162.7
Unfunded Actuarial Liability (UAL)	$544.7	$297.9	$369.4
Funded Ratio (AVA/AL)	68.1%	79.6%	75.9%
Group A Total Normal Cost	37.9%	31.2%	31.9%
Group B Total Normal Cost			25.9%

*City of Austin Group B Long-Term Normal Cost is 8.91%

FUNDING STRUCTURE

Funding Goals

- Move away from the fixed contribution rate model
- Base funding on Actuarially Determined Contribution (ADC)
- Provide safeguards to both the Fund and City on contribution increases or decreases

ADC with Corridor

- Similar to previous funding reforms in other Texas municipalities
- Projected City Contribution rate for the next 30 years is initially established as the target
  - This target becomes the "Corridor Midpoint"
- The annual contribution rate for the City will fall within a range (or corridor) around the Corridor Midpoint

FUNDING STRUCTURE

Funding Process

- Similar to other Austin retirement systems
- Corridor midpoint will be established initially
- Transition period of three years
- Fund will determine the annual ADC, and City will have the opportunity to review with its own actuary and comment
- Fund will determine actuarial assumptions in connection with experience study, and City will have opportunity to review with its own actuary and comment

FUNDING STRUCTURE

Important Differences from Other Austin Plans

- Corridor based on a percentage of the ADC or a wider flat percentage
- No effect to contributions or benefits once corridor is breached
  - No increased member contributions if high end of corridor is breached---Member contribution rate is already one of highest in Texas
  - As a result, no feature added for contribution relief or benefit increases if low end of corridor breached

LEGACY UNFUNDED ACTUARIAL LIABILITY (UAL)

- Legacy UAL based on December 31, 2024 actuarial valuation reflecting:
  - Any plan changes included as part of the V-FSRP
  - Actuarial Value of Assets reset to Market Value of Assets as of December 31, 2024*
  - Assumes 2.5% payroll growth assumption
  - Three-year transition to full ADC
  - Legacy UAL payments are fixed dollar amounts

*Future asset experience will be smoothed based on the asset smoothing method adopted by the Board. The current asset smoothing method spreads asset gains and losses over five years.

LEGACY UAL PAYMENTS

Year Ending		Legacy UAL		UAL Payment During Fiscal Year	
12/31/2024	$	385.9	$	-	*
12/31/2025		403.3		-	*
12/31/2026		416.5		15.7	
12/31/2027		424.4		21.8	
12/31/2028		426.1		28.3	
12/31/2029		427.2		29.0	
12/31/2030		427.6		29.7	
12/31/2031		427.3		30.4	
12/31/2032		426.1		31.2	
12/31/2033		424.1		32.0	
12/31/2034		421.1		32.8	
12/31/2035		417.1		33.6	
12/31/2036		411.9		34.4	
12/31/2037		405.4		35.3	
12/31/2038		397.5		36.2	
12/31/2039		388.1		37.1	
12/31/2040		377.0		38.0	
12/31/2041		364.2		39.0	
12/31/2042		349.4		39.9	
12/31/2043		332.5		40.9	
12/31/2044		313.3		42.0	
12/31/2045		291.7		43.0	
12/31/2046		267.3		44.1	
12/31/2047		240.0		45.2	
12/31/2048		209.5		46.3	
12/31/2049		175.7		47.5	
12/31/2050		138.1		48.7	
12/31/2051		96.5		49.9	
12/31/2052		50.6		51.1	
12/31/2053		-		52.4	

* Payments based on current fixed rate of 22.05%.

The UAL payment as a percentage of payroll* is estimated to be:

2026	13.0%
2027	17.6%
2028-2053	22.2%

* Assumes 2.5% increase per year

ACTUARIALLY DETERMINED CONTRIBUTION

(without modification)

Actuarially Determined Contribution (ADC) equals the sum of three pieces:

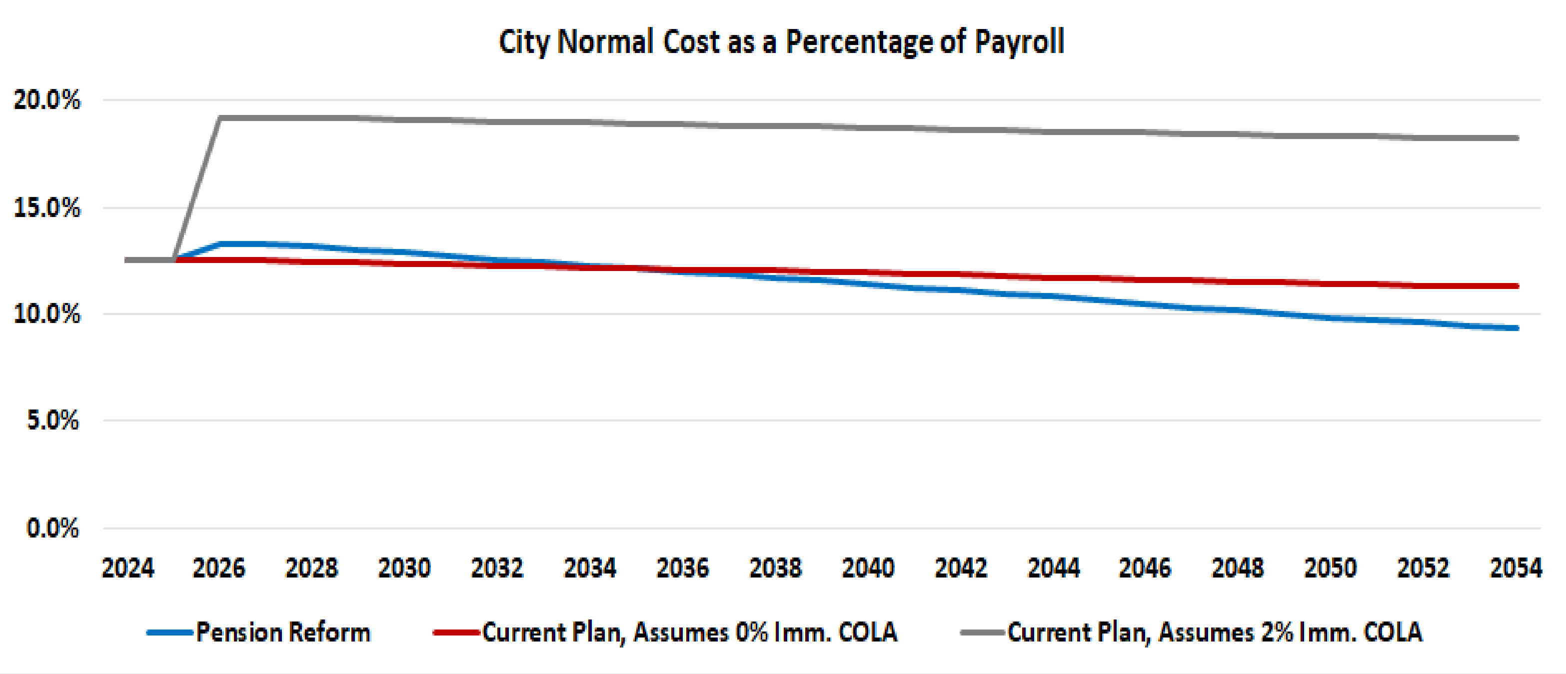
Component	Description
Normal Cost	Based on the Individual Entry Age actuarial cost method
Administration Expenses	Based on the adopted assumption by the Board, currently at 1.25% of payroll
Amortization of UAL	28-year amortization for legacy liability* and 20-year amortization of future UAL from plan experience and assumption changes

* Based on dollar amount schedule determined with the December 31, 2024 actuarial valuation.

TRANSITION TO ADC

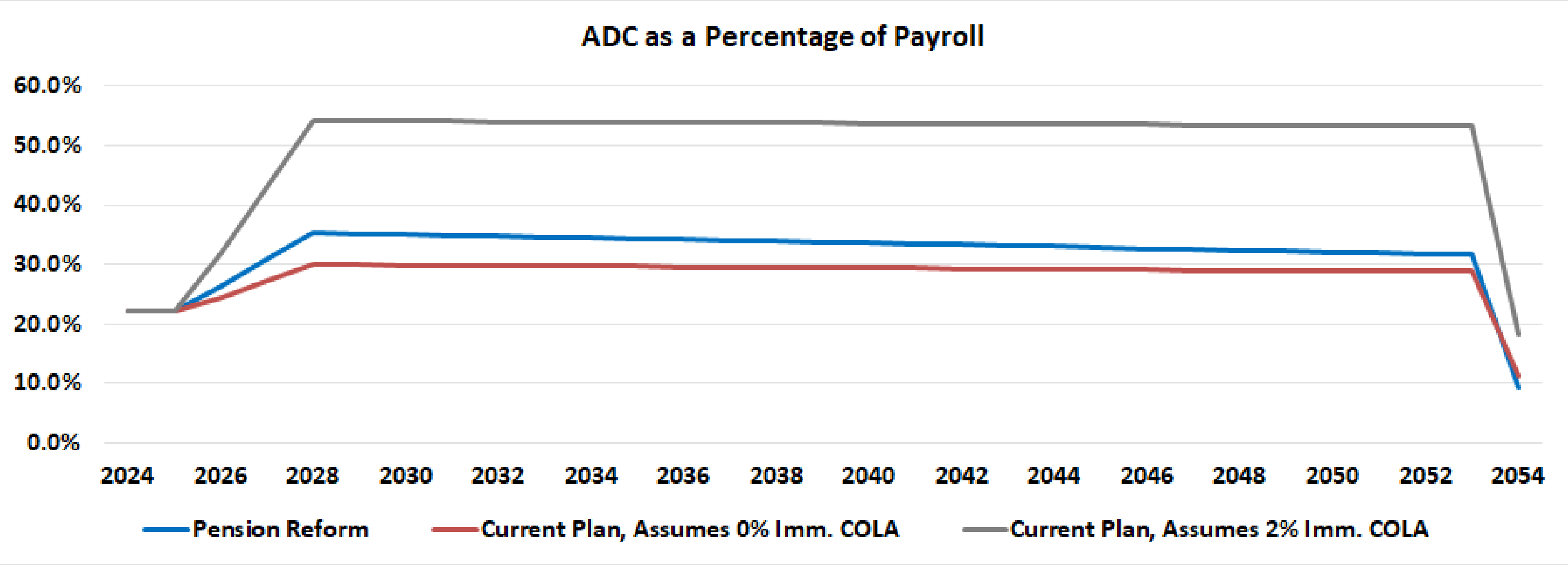
- First effective for the December 31, 2024 actuarial valuation, which impacts the 2026 calendar year contributions
  - 2026 and 2027 calendar year contributions will reflect a transition amount to the full ADC
  - 2028 calendar year contribution will reflect a full ADC contribution
- The Legacy UAL payment will increase by more than 2.5% for the initial years due to the transition to paying the full ADC

COST PROJECTIONS – CITY NC %



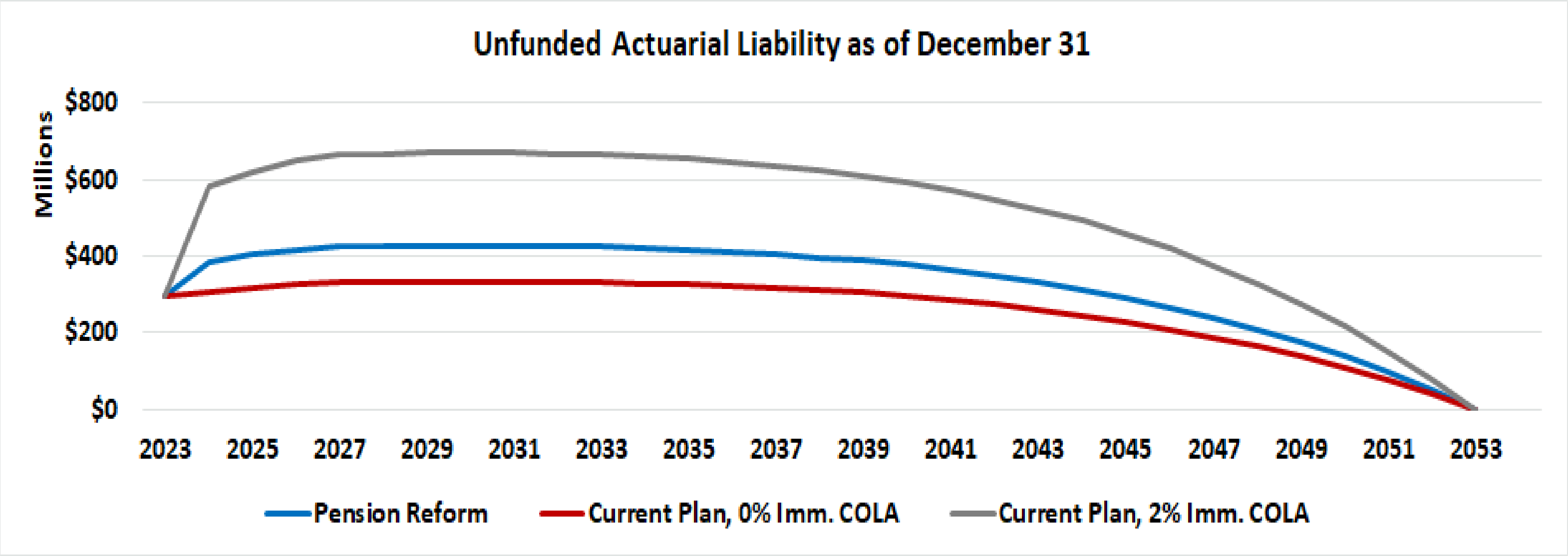
	Calendar Year					
City NC %	2026	2027	2028	2035	2045	2054
Pension Reform	13.3%	13.3%	13.2%	12.1%	10.7%	9.4%
Current Plan, 0% Imm. COLA	12.5%	12.5%	12.5%	12.2%	11.7%	11.3%
Current Plan, 2% Imm. COLA	19.2%	19.2%	19.2%	18.9%	18.5%	18.2%

COST PROJECTIONS – ANNUAL CITY COSTS



			Calendar Year			
ADC	2026	2027	2028	2035	2045	2054
Pension Reform	26.3%	30.8%	35.4%	34.3%	32.8%	9.3%
Current Plan, 0% Imm. COLA	24.5%	27.2%	29.9%	29.6%	29.1%	11.3%
Current Plan, 2% Imm. COLA	32.1%	43.0%	54.2%	53.9%	53.6%	18.2%

COST PROJECTIONS – UAL



	Unfunded Actuarial Liability as of December 31					
UAL	2026	2030	2035	2040	2050	2053
Pension Reform	$416.5	$427.6	$417.1	$377.0	$138.1	$0.0
Current Plan, 0% Imm. COLA	$327.5	$335.1	$326.8	$295.5	$108.2	$0.0
Current Plan, 2% Imm. COLA	$649.2	$671.1	$654.6	$591.8	$216.7	$0.0

APPENDIX

PRB PRINCIPLES OF RETIREMENT PLAN DESIGN

1. Public employers should offer a retirement benefit, and participation in the employer-sponsored primary retirement plan should be mandatory.
2. Contributions to retirement plans should be consistent with the PRB *Pension Funding Guidelines.*
3. Employers and employees should share the cost of the benefit.
4. Retirement plan vesting should occur over a short period, preferably five years of less.
5. Benefits should be designed to place employees on the path to financial security in retirement in consideration of participation or nonparticipation in Social Security.
6. A primary retirement plan should require annuitization of a substantial portion of retirement benefits.
7. In the absence of an immediate and heavy financial need, a retirement benefit should be used only for retirement.
8. Retirement benefits should be protected against the erosion of the benefit's value due to inflation; such benefits should not exceed actual inflation and should be funded in accordance with the PRB *Pension Funding Guidelines*.
9. Employers should provide death and disability benefits.
10. Employers are encouraged to offer plans that are supplemental to the primary retirement plan.
11. Retirement plan governance should represent the interests of all stakeholders, respect fiduciary standards, and be transparent and publicly accountable.
12. Retirement plan assets should be pooled and professionally invested according to prudent investor standards, giving careful consideration to cost.

Source: *https://www.prb.texas.gov/wp-content/uploads/2018/06/Principles-of-Retirement-Plan-Design.pdf*

COA REFORM PRINCIPLES

A. Honor benefit promises to greatest extent possible
B. Maintain prudent actuarial assumptions and long-term affordability
C. Employees and plan sponsor share in system sustainability and risk
D. Actuarially determined funding approach for City Contributions
E. Enact more restrictive requirements for implementing future COLAs and benefit enhancements
F. Establish more balanced board composition
G. To the extent reforms are implemented, they should be implemented equitably across the systems

Source: ***Retirement System Reforms*** *December 11, 2022*

WORKING GROUP GOALS

Benefit Security

Ensuring the Fund has sufficient assets to preserve the ability to pay promised benefits; thereby providing our members with a clear path to achieving retirement security. Our members do not participate in Social Security and AFRF benefits are the only source of retirement income that they have.

Benefit Adequacy

Ensuring the Fund delivers an adequate level of benefits to our members, so they have a decent standard of living in retirement.

Cost Of Living Adjustment (COLA)

Striving to provide COLAs to provide purchasing power protection to retirees to ensure continued benefit adequacy while acknowledging the potential need for adjustments under exceptional circumstances. The Fund has had a well-developed and articulated COLA policy to self-regulate.

Equitable Contribution and Benefit Arrangement across the three Austin Systems

In considering pension reform, recognizing that:

- AFRF has a history of managing the funding health of the plan extremely responsibly. The Fund should be recognized for its good stewardship and not be penalized. In fact, the Fund has a long history of the Board and its active and retired members jointly cooperating to take appropriate action when needed, including increasing member contributions significantly, foregoing COLAs for over a decade, and adopting a responsible COLA policy that has resulted in the discontinuance of COLAs at current funding levels.

- Unlike the members of the other two systems, AFRF members do not participate in Social Security, and any reforms should consider this key difference.

Actuarially Determined Pension Funding Commitment

Ensuring that all benefits for current and future members are consistently and adequately funded through an actuarial determination of required City contributions. Any actuarially determined funding for City contributions should include appropriate determination of the portion of the liability that represents the “legacy liability.”

Fund Sustainability

Continue the almost 50-year history of active and retired members and the plan sponsor sharing in the burden of ensuring Fund sustainability.

Board Composition

Continued recognition of the stewardship and commitment to the Fund by the membership through maintaining a **member-majority board** while recognizing the need for significant City representation by allowing the mayoral position to be filled by either the mayor or a mayoral designee.

RELIANCE

The presentation was prepared solely for the use of the Working Group of the Austin Firefighters Retirement Fund and the City of Austin. Other users of this presentation are not intended users as defined in the Actuarial Standards of Practice, and Cheiron assumes no duty to or liability to such other users.

Data, Methods, and Assumptions

In preparing this presentation, we relied on information, some oral and some written, supplied by the Austin Firefighters Retirement Fund. This information includes, but is not limited to, the plan provisions, employee data, and financial information. We performed an informal examination of the obvious characteristics of the data for reasonableness and consistency in accordance with Actuarial Standard of Practice No. 23.

The actuarial assumptions, data, and methods for the preparation of this report are summarized in the Actuarial Valuation Report as of December 31, 2023, unless noted within this presentation. The assumptions reflect our understanding of the likely future experience of the Fund, and the assumptions as a whole represent our best estimate for the future experience of the Fund. The results of this presentation are dependent upon future experience conforming to these assumptions. To the extent that future experience deviates from the actuarial assumptions, the true cost of the Fund could vary from the results contained within this report. Please also see the Actuarial Valuation Report as of December 31, 2023 for an assessment of risk. Section II of the actuarial report identifies the primary risks to the Fund, including background information and assessment of risk.

Certification and Reliance Statements

The cost estimates for the current and alternative plan designs depend on the assumptions used. For what has been used in this presentation, see the Data, Methods, and Assumptions section above.

RELIANCE

It is imperative to recognize that the analysis provided in this report is based on models estimating such impact. The actual cost of any benefit change will be based on the actual benefits paid by the Fund. As such, if any of the design alternatives are adopted, the ultimate actual financial impact of the plan change will be based on the characteristics and behavior of members actually availing themselves of the adopted change. Thus, the greater the deviations between the actual experience and that assumed in this analysis, the more the costs actually incurred by the Fund may differ. The scope of the assignment resulting in this report does not include either qualitative or quantitative information on how actual costs may vary from those estimated.

Future actuarial measurements may differ significantly from the current measurements in this presentation due to such factors as the following: plan experience differing from that anticipated by the economic or demographic assumptions, changes in economic or demographic assumptions, and changes in plan provisions or applicable law. Actuarial valuations are dependent on assumptions about future economic and demographic assumptions. Actual future experience will never conform precisely to the assumptions and may differ significantly. This deviation is a risk that pension plan sponsors undertake in relying on a pension plan's actuarial valuation results. Please see the Fund actuarial reports for more information related to these risks to the Fund.

This presentation and its contents have been prepared in accordance with generally recognized and accepted actuarial principles and practices and our understanding of the Code of Professional Conduct and applicable Actuarial Standards of Practice set out by the Actuarial Standards Board as well as applicable laws and regulations. Furthermore, as credentialed actuaries, we meet the Qualification Standards of the American Academy of Actuaries to render the opinion contained in this presentation. This presentation does not address any contractual or legal issues. We are not attorneys, and our firm does not provide any legal services or advice.

Elizabeth Wiley, FSA, EA, MAAA, FCA
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Principal Consulting Actuary

ACTUARIAL ASSUMPTIONS AND METHODS

The following summarizes actuarial assumptions and methods that are not described in the actuarial valuation report as of December 31, 2023 and were used in the development of this presentation except where explicitly noted in this presentation.

1. Existing DROP Balances

   Members with existing DROP balances are assumed to withdraw their balances over the next 3 years, but not later than age 70 ½.

2. Pension Reform

   Non-grandfathered active members are assumed to choose the most valuable benefit between the DROP with no COLA and a regular retirement with the 1% automatic deferred COLA. Grandfathered active members are assumed to retire with a DROP and withdraw their balance at the earlier of the valuation assumption and age 62 to be eligible for the 1% COLA deferred to age 67. All current inactives are assumed to receive the 1% deferred COLA beginning at the latest of age 62, 5 years of retirement, and January 1, 2027.

3. Actuarial Value of Assets

   The Actuarial Value of Assets (AVA) is assumed to reset to the Market Value of Assets (MVA) as of December 31, 2024, estimated based on the MVA as of December 31, 2023 and the assumed 7.3% return for the year, and prospectively from December 31, 2024 based on the smoothing method described in the Actuarial Valuation Report as of December 31, 2023.

4. Amortization Method

   The actuarially determined contribution is based on a closed, level percentage of pay amortization assuming 2.5% payroll growth. The legacy UAL and any future UAL are amortized over 28 and 20 years, respectively.

5. New Hires

   New hire costing is based on a new entrant profile reflecting new members joining the Fund in 2022 and 2023. The profile reflects an average hire age of 29 years and pay of $60,338.