COAERS
CITY OF AUSTIN
EMPLOYEES' RETIREMENT SYSTEM

Board Approved Policy

Subject:	Funding
Review Committee:	Benefits and Services Committee
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Signature of Chairperson:

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CITY OF AUSTIN EMPLOYEES' RETIREMENT SYSTEM
BOARD APPROVED POLICY
FUNDING POLICY

I. PURPOSE AND SCOPE

This Funding Policy ("Policy") is designed as a guideline to communicate the Board of Trustees' position on the City of Austin Employees' Retirement System (COAERS) long-term funding goals, determine appropriate methods for COAERS to achieve a 100% funded ratio as required by Texas Government Code, Section 802.2011, establish appropriate actuarial assumptions and methodologies, provide guidelines for benefit and contribution policy recommendations, and establish a process to monitor and report on COAERS' funding progress. COAERS is formally adopting certain baseline actuarial measurements to provide guidance for actuarial valuations performed on and after December 31, 2020.

II. FUNDING GOALS AND OBJECTIVES

The goal of this Policy is to develop a long-term strategy that ensures COAERS achieves its mission of providing reliable retirement benefits. To achieve this outcome, the Board of Trustees establishes the following objectives of this Policy:

- Ensure the security of vested accrued benefits by making that certain contributions and assets are sufficient to pay benefits when due.
- Achieve long-term full funding (funded ratio of 100% or greater) of the cost of promised benefits.
- Ensure that each generation of members and employers incurs the cost of benefits for the employee who provide services to them, rather than deferring those costs to future members and employers.
- Manage and control contribution rate volatility to the extent reasonably possible, consistent with other Funding Policy goals and objectives.
- Provide a reasonable margin for adverse experience to help offset the risks inherent in managing COAERS.
- Eliminate negative amortization as quickly as possible and maintain a contribution rate above the threshold that results in negative amortization.
- Support transparency and accountability to the stakeholders of COAERS.

III. DEFINITIONS

“Actuarial accrued liability” (AAL) means the actuarial accrued liability determined in accordance with the Actuarial Cost Method outlined this Policy.

“Actuarial value of assets” (AVA) means the Plan’s assets determined in accordance with the Asset Valuation Method outlined in this Policy.

“Actuarially Determined Employer Contribution Rate” (ADEC rate) means the contribution rate that pays for the Normal Cost plus amortizes the Unfunded Actuarial Accrued Liability over the Benchmark Funding Period, expressed as a percentage of payroll.

“Actual employer contribution rate” means the actual employer contribution paid by the City of Austin currently under the Amended Supplemental Funding Plan or by agreement.

“Benchmark Funding Period” means the length of time required to eliminate the System’s unfunded liability as established in this Policy.

“Benefit enhancement” means any change to the current benefit policy for retired, active, vested, and non-vested members of the System which increases the actuarially determined contribution rate, increases the amortization period, or decreases the funded ratio of the System. Examples include but are not limited to benefit formula multiplier increases, reductions in eligibility for benefits, cost of living adjustments, or lump-sum additional benefit payments to retired members or beneficiaries.

“Board of Trustees” means the Board of Trustees of the City of Austin Employees’ Retirement System as defined by Vernon's Texas Civil Statute Article 6243n.

“Cost Method” means the actuarial method of allocating the Present Value of Projected Benefits into past and future periods.

“Cost of living adjustment” (COLA) means an adjustment which is added to the current monthly payment of the retirement annuities, pensions, or allowances of each retired member and beneficiary to help counteract the erosion of purchasing power caused by inflation.

“Funded ratio” means the value of a System’s assets, expressed as a percentage of the plan's actuarial liability

“Funding Period” means the projected number of years to fully amortize the Unfunded Actuarial Accrued Liability assuming the current employer and employee contribution rates continue, and all future experience aligns with the underlying actuarial valuation assumptions.

“Normal Cost” (NC) means the portion of the total Present Value of Future Benefits that is allocated to a valuation year by the actuarial cost method as outlined in this Policy plus the annual assumed administrative expenses.

“Plan Sponsor” means the City of Austin.

“System” means the City of Austin Employees’ Retirement System and the provisions found in Vernon's Texas Civil Statute Article 6243n.

“Statutory employer contribution rate” means the employer contribution rate as defined by Vernon's Texas Civil Statute Article 6243n, which is currently eight percent (8%) of base compensation.

“Total Present Value of Projected Benefits” (PVPB) means the actuarial present value of all benefits expected to be paid from the Fund for all current members and beneficiaries.

“Unfunded Actuarial Accrued Liability” (UAAL) means the excess of the actuarial accrued liability above the actuarial value of assets.

IV. ROLES AND RESPONSIBILITIES

COAERS exists for the exclusive benefit of its members, beneficiaries, and retirees. This “exclusive benefit” rule shall be strictly followed when making, implementing, and monitoring funding policy decisions and specific care should be taken to maximize alignment of COAERS stakeholders while mitigating the conflicts of interest and agency problems that may arise.

Board of Trustees

The Board has the fiduciary duty of overseeing the System and ensuring the security of vested accrued benefits in accordance with the State Constitution and State Law. The Board is required by the State Constitution and State Law to select an actuary and adopt sound actuarial assumptions to be used by the System. The Board is also required by State Law to conduct an actuarial valuation annually and an actuarial experience study at least every five years.

The Board is also required to develop a written funding policy that details the Board’s plan for achieving a funded ratio of that is equal to or greater than 100% and file a copy with the City of Austin. In fulfilling this responsibility, the Board will establish and monitor System funding in accordance with the goals and objectives stated in this Policy and take actions as necessary in accordance with this Policy.

Benefits and Services Committee

The Benefits and Services Committee is chartered to assist the Board of Trustees in fulfilling its fiduciary oversight responsibility of the System. Duties of the Benefits and Services Committee may include, but are not limited to:

- Annually review and recommend action on the System's actuarial valuation report.
- Review the actuarial experience of the System.
- Review and recommend actuarial assumptions and methodologies.
- Review the results of all actuarial audits.
- Review and make recommendations for Plan revisions.

Executive Director

The Executive Director is responsible for reporting to the Board and the Benefits and Services Committee in accordance with this Policy.

Actuarial Consultant(s)

The Actuarial Consultant retained by the Board shall provide and present the annual actuarial valuation in accordance with the actuarial methods as outlined in this Policy and as adopted by the Board from time to time.

Plan Sponsor

Every five years, the City of Austin is required by State Law to conduct an audit of the System's most recent annual actuarial valuation.

V. ACTUARIAL METHODS AND ASSUMPTIONS

The Board adopts the following actuarial cost methods for the purposes of actuarial valuations occurring on and after December 31, 2020.

A. Asset Valuation Method – Five-year smoothing with direct offset of gains/(losses) against the expected market value of assets and 20% soft corridor
B. Actuarial Cost Method – Entry Age Normal (Individual)
C. Funding Period – Determined based on an open group projection

All actuarial assumptions adopted by the Board are listed in Appendix A of this Policy.

VI. COAERS STATUTE AND CONTRIBUTION POLICY

COAERS is governed by to Vernon's Texas Civil Statutes, Article 6243n under which both the member and City contribution rates are set at 8% of base compensation. The City may elect to increase its contribution rate above the statutory rate and the members may increase the employee contribution rate by a majority vote of all such members voting at an election to consider an increase in contributions. The Board, however, may not unilaterally change contribution rates.

VII. FUNDING POLICY PRINCIPLES

For each valuation, the Board will require the disclosure of the ADEC rate to assess the System's funded status, trend in funding progress, and assess the need for changes in the current contribution rates, potential changes to benefits, or a combination thereof. The ADEC rate is the percent of payroll calculated to pay the Normal Cost (including administrative expenses) plus the amount needed to amortize the UAAL over the Benchmark Funding Period. Each future valuation will establish either a liability gain layer or a liability loss layer. These layers will represent unexpected increases or decreases in the UAAL. New gain and loss layers will be amortized over a 15-year closed period. The amortization layers will begin one year after the valuation date using a level percentage of payroll amortization method.

The Benchmark Funding Period is set at an initial 25-year closed period beginning with the December 31, 2020 actuarial valuation. If total contributions to the System are enough to satisfy the ADEC rate, the existing UAAL on December 31, 2020 will be fully funded within 25 years and the System will achieve a 100% funded ratio. Once the System achieves a funded ratio of 100% or greater, the ADEC rate should never be lower than the statutory employer contribution rate.

If the actual Funding Period exceeds the Benchmarking Funding Period for two consecutive actuarial valuations or the actual Funding Period exceeds the maximum funding period established in the Pension Review Board Funding Guidelines for one actuarial valuation, the Board will notify the City and COAERS' membership. Additionally, the Board will work with the City to consider modifications to contribution and benefit policies to return the Funding Period to the Benchmark Funding Period.

The following framework will guide consideration of changes to contribution and benefit policies to return the Funding Period to within the Benchmark Funding Period:

- Enact a more flexible contribution policy to manage the risks of the System and pay the unfunded actuarial accrued liability and normal cost of the System over an appropriate time-period.
- To the extent necessary, amend benefit policies to ensure that the System's obligations can be met for all generations of COAERS members.
- Utilize appropriate risk-sharing between the City and employees to manage the risks inherent in funding a defined benefit plan.

VIII. GUIDELINES FOR FUTURE COST OF LIVING ADJUSTMENTS

The Board establishes the following conditions for when the Board would consider supporting cost of living adjustments:

A. The adjustment can be financially supported by contributions to the System on a regular, periodic basis preferably on an annual basis but no less frequently than every five years.

B. The funded ratio of the Plan is greater than or equal to 80% after incorporating the cost of living adjustment, assuming it to be regular and periodic.

C. The amortization period for unfunded liabilities is less than or equal to 20 years after incorporating the cost of living adjustments, assuming it to be regular and periodic.

D. The actual employer contribution rate is greater than or equal to the ADEC rate after incorporating the cost of living adjustments, assuming it to be regular and periodic.

E. The Board has reviewed sensitivity and stress testing analysis as to the impact to the System's amortization period and funded ratio of providing a cost of living adjustment should certain assumptions including rate of return and payroll have adverse future experience.

IX. GUIDELINES FOR FUTURE BENEFIT ENHANCEMENTS AND ADDITONAL PAYMENTS

For all other benefit enhancements and additional payments, the Board establishes the following conditions for when the Board would consider supporting such enhancements:

A. Annual cost of living adjustments are built into funding assumptions.
B. The funded ratio is equal to or greater than 120% after incorporating the benefit enhancement.
C. The ADEC rate is equal to the statutory employer contribution rate.
D. The Board has reviewed sensitivity and stress testing analysis as to the impact to the System's amortization period and funded ratio of the benefit enhancement or additional payment should certain assumptions including rate of return and payroll have adverse future experience.

X. GUIDELINES FOR FUTURE REDUCTIONS IN EMPLOYER CONTRIBUTION RATES

The Board of Trustees believes that it is best to consider supporting a reduction in the actual employer contribution rate only when the following conditions exist:

A. Annual cost of living adjustments are built into funding assumptions; and
B. The funded ratio will remain greater than or equal to 105% subsequent to any reduction in the actual employer contribution rate.
C. The actual employer contribution rate should not go down by more than 1% of pay per year.
D. The Board has reviewed sensitivity and stress testing analysis as to the impact to the System's amortization period and funded ratio of the reduction in the employer contribution rate should certain assumptions including rate of return and payroll have adverse future experience.

XI. AMENDED SUPPLEMENTAL FUNDING PLAN

A. This Policy is to be implemented consistently with City of Austin Resolution No. 20100913-008 as known as the Amended Supplemental Funding Plan.

B. So long as the Amended Supplemental Funding Plan remains in effect, any future benefit enhancements or cost of living adjustments otherwise permitted under the System's governing documents will require recommendation from the City Manager and approval by the City Council.

C. Any such recommendation by the City Manager should include an actuarial analysis by COAERS actuarial consultant of the effect of the requested enhancement or adjustment on the Plan and the level of employer contributions to the System, including sensitivity and stress testing analysis as to the impact to the System's amortization period and funded ratio of providing the cost of living adjustment or benefit enhancement should certain assumptions including rate of return and payroll have adverse future experience.

XII. MONITORING AND EVALUATION

A. The Board of Trustees will monitor COAERS' progress towards the goals and objectives established in this Policy at least annually.

B. The Executive Director and COAERS' actuarial consultant will annually report to the Board on progress toward meeting the goals and objectives established in this Policy by reviewing key metrics and funding trends including but not limited to the ADEC, funded ratio, funding period, actual returns compared to the assumed rate of return, UAAL as a percentage of payroll, active to retired ratio, negative amortization, cash flow, and duration of accrued liability. The report shall also include review of contribution and benefit policy modifications if necessary consistent with this Policy.

C. Annually, COAERS will present a report to the City of Austin on progress toward meeting the goals and objectives established in this Policy including information as detailed in this section of the Policy.

D. The Benefits and Services Committee will review this Policy at least every two years and make recommendations to the Board necessary to maintain progress towards the goals and objectives in this Policy.

APPENDIX A: ACTUARIAL ASSUMPTIONS

The most recent experience study was completed based on data collected through December 31, 2018. The Board adopted the assumptions outlined below to be effective with the December 31, 2019 actuarial valuation. Please see our Experience Study report dated December 2019 to see more detail of the rationale for the current assumptions. As authorized under Article 6243n of the Vernon's Civil Statutes of the State of Texas, actuarial assumptions and methods are set by the Board of Trustees, based upon recommendations made by the plan's actuary.

A. ACTUARIAL ASSUMPTIONS

1. Investment Return Rate (adopted effective December 31, 2019)

   7.00% per annum, compounded annually, composed of an assumed inflation rate of 2.50% and a real rate of return of 4.50%, net of investment expenses.

2. Mortality

   a. Nondisabled annuitants (adopted effective December 31, 2019)

      Healthy retirees and beneficiaries – The Pub-2010 Healthy General Tables for males and females with full generational projection assuming immediate convergence of rates in the mortality projection scale MP-2018, 2D for male and female. Mortality improvement is projected from the mortality table's base year of 2010 (see Item 20 for further discussion of mortality improvement).

   b. Disabled annuitants (adopted effective December 31, 2019)

      Disabled annuitants – The Pub-2010 Healthy General Tables for males and females, set forward three years with full generational projection assuming immediate convergence of rates in the mortality projection scale MP-2018, 2D for male and female. Mortality improvement is projected from the mortality table's base year of 2010 (see Item 20 for further discussion of mortality improvement). A minimum 3% rate of mortality applies at all ages.

   c. Active members (adopted effective December 31, 2019)

      Active employees – The Pub-2010 Employees General Tables for males and females with full generational projection assuming immediate convergence of rates in the mortality projection scale MP-2018, 2D for male and female. Mortality improvement is projected from the mortality table's base year of 2010 (see Item 20 for further discussion).

Note regarding mortality table extensions:

Pub-2010 mortality tables are not inclusive of all ages. Mortality rates for active members were extended above age 80 by a constant exponential rate to the Healthy Retiree rate at age 100. Mortality rates for nondisabled annuitants below age 50 were extended using a constant exponential rate to the Juvenile rates. Disabled annuitant mortality rates were extended below age 18 using a constant exponential based on the age 18 and 24 mortality rates.

3. Retirement Rates: **(adopted effective December 31, 2019)** The following rates of retirement are assumed for members eligible for normal retirement.

Age	Rates of Retirement	
	Males	Females
44 & under	22.0%	25.0%
45	20.0%	20.0%
46	20.0%	20.0%
47	20.0%	20.0%
48	20.0%	20.0%
49	20.0%	20.0%
50	22.0%	24.0%
51	22.0%	24.0%
52	22.0%	24.0%
53	22.0%	24.0%
54	22.0%	24.0%
55	21.0%	26.0%
56	21.0%	26.0%

57	21.0%	26.0%
58	21.0%	26.0%
59	21.0%	26.0%
60	22.0%	21.0%
61	22.0%	21.0%
62	27.0%	24.0%
63	18.0%	16.0%
64	18.0%	16.0%
65	18.0%	24.0%
66	30.0%	24.0%
67	30.0%	26.0%
68	22.0%	26.0%
69	22.0%	26.0%
70	30.0%	26.0%
71	22.0%	24.0%
72	22.0%	24.0%
73	22.0%	24.0%
74 & older	100.0%	100.0%

Group B members are assumed to retire at twice the applicable rate upon the first year they attain eligibility for normal retirement. Early retirement rates (of 1% at age 55 increasing by 1% every two years to 5% at ages 63 and 64) apply for Group B members.

4. Rates of Decrement Due to Withdrawal (adopted effective December 31, 2019)

Rates of withdrawal are comprised of a select period for the first 5 years of employment and ultimate rates based on years of service from retirement after the end of the select period. The following rates during the select period apply at all ages during the applicable year of employment:

Years of Employment	Males	Females
1	0.1100	0.1600
2	0.1050	0.1500
3	0.0925	0.1275
4	0.0675	0.1000
5	0.0600	0.0850

After the select period ends, rates of withdrawal are based on the number of years from retirement. The rates are shown below for males and females

Years from Eligibility for Unreduced Retirement	Rates of Withdrawal After Select Period	
	Males	Females
1	0.0120	0.0080
2	0.0120	0.0175
3	0.0120	0.0175
4	0.0120	0.0200
5	0.0150	0.0200
6	0.0200	0.0200

7	0.0200	0.0250
8	0.0200	0.0250
9	0.0200	0.0250
10	0.0250	0.0300
11	0.0300	0.0350
12	0.0350	0.0375
13	0.0400	0.0400
14	0.0450	0.0700
15+	0.0560	0.0825

5. Disability Rates* (adopted effective December 31, 2015)

   Sample rates are shown below:

Age	Rates of Decrement Due to Disability Males and Females
20	0.000004
25	0.000025
30	0.000099
35	0.000259
40	0.000494
45	0.000804
50	0.001188
55	0.001647
60	0.002180

* Rates are for disability due to all causes; occupational disability rates are assumed to be 10% of all causes.

6. Rates of Salary Increase (adopted effective December 31, 2019)

Years of Service	Promotional Rate of Increase	Total Annual Rate of Increase Including 2.50% Inflation Component and 1.00% Productivity Component
1 – 3	2.25%	5.75%
4 – 5	2.00%	5.50%
6	1.75%	5.25%
7	1.50%	5.00%
8	1.25%	4.75%
9 – 10	1.00%	4.50%
11 – 12	0.75%	4.25%
13 – 14	0.50%	4.00%
15 – 16	0.25%	3.75%
17+	0.00%	3.50%

7. DROP Participation: (adopted effective December 31, 2019)

   It was assumed that 15% of retiring active members with at least 20 years of service would elect a “Backward” DROP. It is assumed that all members who Back Drop will elect to DROP back to the date that would provide the greatest actuarial value to the member.

8. Married Percentage: (adopted effective December 31, 1997)

   100% of the active members are assumed to be married.

9. There will be no recoveries once disabled: (adopted effective December 31, 1997)

10. Spousal Age Difference: (adopted effective December 31, 2012)

    Males are assumed to be three years older than females.

11. Normal Form of Payment: (adopted effective December 31, 1997)

    It is assumed that all retiring members will elect the Life only form of payment with a guaranteed return of accumulated employee contributions.

12. Crediting Rate on Employee Contributions: (adopted effective December 31, 2002)

    It is assumed that the interest credit rate on employee contributions will be 6.0%.

13. Individual salaries used to project benefits: (adopted effective December 31, 1997)

    Rates of pay as of the valuation date are reported for all employees.

14. Pay increase timing: (adopted effective December 31, 1997)

    Middle of calendar year.

15. Decrement timing: (adopted effective December 31, 1997)

    Decrements of all types are assumed to occur mid-year.

16. Eligibility testing: (adopted effective December 31, 2002)

    Eligibility for benefits is determined based upon the age nearest birthday and service nearest whole year on the date the decrement is assumed to occur.

17. Decrement relativity: (adopted effective December 31, 2002)

    Decrement rates are used directly from the experience study, without adjustment for multiple decrement table effects.

18. Incidence of Contributions: (adopted effective December 31, 2002)

    Contributions are assumed to be received continuously throughout the year based upon the contribution rates as a percent of payroll (established in statute or agreed upon under the Supplemental Funding Plan) shown in this report and the actual payroll payable at the time contributions are made.

19. Benefit Service: (adopted December 31, 1997)

    All members are assumed to accrue one year of eligibility service each year.

20. Mortality Improvement:

The base mortality tables are anchored at the year 2010. To account for future mortality improvement, the base mortality rates in Item 2 are projected forward assuming immediate convergence of rates in the mortality projection scale MP-2018, 2D for male and female.

21. Service Purchases (military, permissive, and sick leave conversion):

No service purchases of any type are assumed. Any gains or losses due to these purchases are recognized in the valuation following the purchase.

22. Cost of Living Adjustments and One-time Payments:

No future cost of living adjustments are assumed. In addition, no one-time payments (13th checks) are assumed.

ACTUARIAL VALUE OF ASSETS

The actuarial value of assets is equal to the market value of assets less a five-year phase in of the Excess (Shortfall) between expected investment return and actual income. The expected investment return each year is calculated based on the market value of assets with the difference from actual income smoothed in over five years in 20% increments. If the current year's difference is opposite sign of the prior years' deferred Excesses/(Shortfalls), then the prior years' bases (starting with the oldest) are reduced dollar for dollar along with the current year's base. Any remaining bases are then recognized over five years (20% per year) from their initial creation. This can and will result in some bases being recognized in a period shorter than five years.

If the resulting preliminary asset value is less than 80% or more than 120% of the market value of assets, then 1/3 of the amount outside of the 80% to 120% corridor is recognized in the final actuarial value of assets. In extreme market conditions, this could result in an actuarial value of assets outside of the 80% to 120% market value of assets corridor.

B. ACTUARIAL FUNDING METHOD

The actuarial accrued liability is determined using the Entry Age Normal actuarial cost method. This method assigns the System's total actuarial present value of future benefits to various periods. The actuarial accrued liability is assigned to years prior to the valuation and the normal cost is assigned to the year following the valuation. The remaining costs are assigned to future years.

The normal cost is determined on an individual basis using the Individual Entry Age Normal Cost method. The actuarial accrued liability is the difference between the total present value of future benefits and the actuarial present value of future normal costs where future normal costs are based on the benefit provisions that are applicable to each individual member. The unfunded actuarial accrued liability is the excess of the actuarial accrued liability over the actuarial value of assets.

C. FUNDING PERIOD

The funding period is determined using an open group projection. In the open group projection, the demographic assumptions are applied to the current active employees and any employees that are assumed to leave employment are replaced one for one with a new employee. Over time this results in the change of the employee group from mostly Group A members to Group B members. The projection is built to assume no gains or losses on the actuarial accrued liability or the actuarial value of assets. The funding period is the length of time it takes in the open group projection for the actuarial value of assets to exceed the actuarial accrued liability.

In the projection, new members' pay are assumed to increase at 3.50% year over year (i.e. a new employee in 2020 is assumed to be hired at a salary that is 3.50% greater than a new employee hired in 2019. The 3.50% growth rate is equal to the wage inflation assumption of 3.50% (ultimate salary increase assumption showing in Item A.6.). Note that this is not an assumption that payroll will grow at 3.50% per year. Payroll could grow more slowly in the near-term due to membership demographics.

D. CHANGES IN ASSUMPTIONS AND METHODS

New assumptions were adopted effective December 31, 2019. Please refer to the Actuarial Experience Study report dated December 2019 for more detail on the assumption changes.