CITY OF AUSTIN EMPLOYEES' RETIREMENT SYSTEM
AND CITY OF AUSTIN
FUNDING POLICY
Adopted XYZ, 2024

I. Introduction and Purpose

The City of Austin Employees' Retirement System (COAERS or the "System") is established by Article 6243n, Texas Revised Civil Statutes (the "COAERS statute"). The COAERS statute provides authority for the Board of Trustees to administer the System. The City of Austin (the "City") is the plan sponsor. This policy was jointly developed by the System and the City.

The purpose of this policy is to align with best practices in pension funding, as well as to implement the requirements for public retirement systems in Texas pursuant to Section 802.2011, Texas Government Code.

The primary objective of the funding policy is to establish guidelines intended to produce actions to meet the long-term pension obligations promised to all the members of the System. To achieve this goal, the policy sets forth procedures to pay off any Unfunded Actuarial Accrued Liability (UAAL) over a fixed, closed period and achieve and maintain a funded ratio equal to or greater than 100 percent.

This funding policy is intended to be interpreted consistent with the COAERS statute, which is controlling.

II. Funding Objectives

The primary funding objective of the System is to pay the benefits promised under the System and protected by the Texas Constitution. Additional funding objectives of the System include: (1) maintaining a financially sound benefit plan that attracts future generations of workers; (2) have each generation of members and the City pay the cost of benefits as such benefits accrue; and (3) to ensure the long-term affordability and sustainability of the plan for both members and the City.

Following these objectives, the Texas Legislature amended the COAERS statute (SB1444 in 2023) to establish three primary funding mechanisms to ensure that there is a scheduled payment for paying off the UAAL. First, the COAERS statute establishes a fixed payment schedule for the City to finance the initial UAAL (determined as of December 31, 2022) over a 30-year fixed, closed period, beginning on January 1, 2024 (referred to as the "Legacy Liability").

Second, the COAERS statute provides that the member contribution to the System would equal 10% of pay, phased-in over a two-year period (9% in 2024 and 10% in 2025 and thereafter). Finally, the COAERS statute provides that the City will contribute an actuarially determined employer contribution rate (ADEC), which will be comprised of the employer portion of the normal cost of the System (the normal cost in excess of the member contributions) and an amortization payment (or credit) to fund unanticipated changes in the UAAL over a period of time which initially aligns with the legacy liability payment schedule until that period reaches 20-years, thereafter, a 20-year fixed, closed period; beginning one year after the valuation date on which the unanticipated change in the UAAL is identified (referred to as the City Contribution Rate).

The City Contribution Rate is subject to certain "corridors" as discussed in more detail below. In total, the City contribution each year is comprised of its scheduled payment to the Legacy Liability and the determined City Contribution Rate. If the calculated City Contribution Rate exceeds the upper corridor limit, then the Member Contribution Rate is adjusted to the excess of the calculated City Contribution Rate above the corridor limit, but in no circumstance shall the Member Contribution Rate exceed 12% of pay.

III. Actuarial Valuations, Actuarial Methods, and Experience Studies

Actuarial valuations (referred to in the COAERS statute as the Risk Sharing Valuation Study or "RSVS") will be conducted annually based on data as of December 31 each year, using the assumptions and methods adopted by the Board after each experience study or more frequently if recommended by the System actuary.

The Board will commission a comprehensive actuarial experience study based on data as of December 31, 2023 and then at least every five years thereafter pursuant to COAERS statute and Sec. 802.1014, Texas Government Code.

The City may elect to have its own actuary conduct an independent actuarial experience study or to review the experience study of the System's actuary. To the extent the hypothetical city contribution rates calculated by the System's actuary and the City's actuary differ by more than two percent of pensionable payroll, a reconciliation process is entered into as detailed in the COAERS statute.

Assumptions are based on actuarial standards of practice considering both actual experience and reasonable future expectations. After each experience study, the Board will adopt a set of assumptions for future Risk Sharing Valuation Studies based upon current actuarial standards of practice considering both actual experience and reasonable future expectations.

Key actuarial methods utilized by the System’s actuary include:

- Actuarial cost method: Entry Age Normal Cost (Individual), which allocates the cost of accruing benefits as a level percentage of pay over the period from the member's entry into the plan until their termination or retirement.

- Actuarial asset method: Five-year smoothing method recognizing 20% of the differences between expected and actual investment income in the current and each subsequent year, with offsetting unrecognized gains and losses immediately recognized.

- Amortization Policy: A declining 30-year amortization period is used in determining the payments on unfunded liability layers until reaching 20-years, thereafter, using closed 20-year layers. The aggregate funding period for the system is the weighted average of the amortization layers. The goal is to eliminate negative amortization as soon as possible, but negative amortization is expected to continue until the Legacy Liability payoff schedule reaches 20 years.

IV. Risk Sharing Mechanisms

a. Risk Sharing Valuation Study

Each year an RSVS valuation is performed by the System's actuary. The RSVS valuation will be used to calculate the City Contribution Rate as specified by statute, consistent with the corridor requirements outlined below. This Estimated City Contribution Rate is determined based on the employer normal cost of the System and the amortization payments of the "new" liability layers created after the Legacy Liability was established. The Estimated City Contribution Rate is then compared to the "City Contribution Corridor" to determine the final City Contribution Rate.

b. City Contribution Corridor

As set forth in the COAERS statute, an initial RSVS valuation calculated a City Contribution Corridor for the next 30 years. The mid-point of this corridor was established as the expected normal cost of the System over the subsequent 30-years following the initial RSVS assuming that the active population remains constant and based on the actuarial assumptions and methods as of the initial RSVS. The City Contribution Corridor maximum (or ceiling) for each year is 5% of pay above the corridor mid-point for that fiscal year. The City Contribution Corridor minimum (or floor) for each year is 5% of pay below the Corridor mid-point for that fiscal year but can never be less than zero.

c. Determining the City Contribution Rate

If the Estimated City Contribution Rate determined in connection with the RSVS is within the City Contribution Corridor, then the final City Contribution Rate is equal to the Estimated City Contribution Rate with the following exceptions:

- If the System's funded ratio is less than 90% as determined under the RSVS, then the final City Contribution Rate is the greater of the Estimated City Contribution Rate or the corridor midpoint for that fiscal year, but not to exceed the maximum of the City Contribution Corridor for that fiscal year.

- If the funded ratio is greater than 90% as determined under the RSVS, then the final City Contribution Rate is equal to the Estimated City Contribution Rate, but not to be less than the minimum of the City Contribution Corridor for that fiscal year.

In addition to the City Contribution Rate, the City shall also pay the established Legacy Liability payment. If the System's funded ratio should exceed 100% then the Legacy Liability shall be considered fully paid and no additional Legacy Liability payments shall be made.

The City may contribute an amount in addition to the scheduled Legacy Liability payment to reduce the number or amount of scheduled future Legacy Liability payments. If the City contributes an additional amount, the System’s actuary shall create a new schedule of City Legacy Liability payments that reflects payment of the additional contributions.

d. Determining the Member Contribution Rate

The COAERS statute also provides a risk-sharing component for the active members. The legislation increased the member contribution rate to 10% of pay. However, if the Estimated City Contribution Rate exceeds the City Contribution Corridor maximum, then the member rate shall be increased by the amount the Estimated City Contribution Rate exceeds the City Contribution Corridor maximum, but not by more than an additional 2% of pay.

In subsequent years, the member contribution rate will continue to be adjusted to reflect the excess as determined under the RSVS for that year. If the Estimated City Contribution Rate should again fall below the City Contribution Corridor maximum in a subsequent year, the member rate will decrease back to 10% of pay.

Should the Estimated City Contribution Rate exceed the City Contribution Rate Corridor maximum by more than 2% of pay, the System will promptly notify the City and engage in planning as needed with the City to ensure that continued progress toward the goals of this policy will be made.

V. Changes to Contributions or Benefits

The City and COAERS may agree on a written transition plan for resetting the corridor midpoint, member contribution rates, or employer contribution rates if at any time the funded ratio of the System is equal to or greater than 100% or for any calendar year after the payoff of the Legacy Liability.

Before a cost-of-living-adjustment (COLA) or additional payment to retirees, beneficiaries, or other payees may be provided, the following must occur:

1. The System's actuary must certify in writing that, consistent with the application of sound actuarial assumptions and methods, the System has and will likely continue to have the ability to pay such an amount after all other obligations of the System have been paid;
2. The COAERS Board of Trustees must approve the COLA or additional payment;
3. The City Council must approve the COLA or additional payment; and
4. COAERS statute must be amended by the Texas Legislature to provide for the COLA or additional payment.

VI. Review of the Funding Policy

The System and City will review this policy periodically as necessary.