AGENDA

• Impact of Change in Actuarial Assumptions at HPOPS

• GASB 68 Implementation

• Effect of benefit changes on future plan costs

• Questions
HPOPS Actuarial Assumption Changes

- The cost of a pension plan = the benefits paid minus the net investment income earned.

- To estimate the cost and to determine annual contribution amounts an actuary must make certain assumptions regarding future events:
  - Rate of return on investments
  - Salary increases
  - Turnover
  - Mortality and disability
  - Incidence of retirement

- Assumptions are not static:
  - Should be monitored periodically and changed accordingly
  - Assumption changes do not change the cost – just the timing of contributions

- HPOPS has prudent fiduciary policy to review assumptions every 5 years:
  - Commissioned its actuary to conduct a review in 2014
  - Actuary recommended changes for the actuarial valuation as of July 1, 2014
  - HPOPS board adopted the recommended changes
## Portfolio HPOPS Summary of Significant Assumption Changes

<table>
<thead>
<tr>
<th>Assumption</th>
<th>Change</th>
<th>Impact on Liability</th>
</tr>
</thead>
<tbody>
<tr>
<td>Investment Rate of Return</td>
<td>Reduce from 8.5% to 8.0%</td>
<td>Increase</td>
</tr>
<tr>
<td>Salary Increases</td>
<td>Reduce by 0.5% per year</td>
<td>Decrease</td>
</tr>
<tr>
<td>COLA</td>
<td>Reduce from 2.8% to 2.7%</td>
<td>Decrease</td>
</tr>
<tr>
<td>DROP Interest Rate</td>
<td>Reduce from 7.0% to 6.4%</td>
<td>Decrease</td>
</tr>
<tr>
<td>DROP/PROP Payout</td>
<td>From Immediate to 10 Year</td>
<td>Decrease</td>
</tr>
<tr>
<td>Turnover</td>
<td>Lower Slightly</td>
<td>Increase</td>
</tr>
<tr>
<td>Mortality</td>
<td>Update for Improved Mortality</td>
<td>Increase</td>
</tr>
<tr>
<td>Incidence of Retirement</td>
<td>Increased Expected Age at Retirement by About 1 Year</td>
<td>Decrease</td>
</tr>
</tbody>
</table>
HPOPS – Impact on Funding

• City contribution schedule set by Meet & Confer Agreement:
  o $113 million for FY 2015
  o Increases by $10 million each year in future
  o Additional contribution if Funded Ratio (current assets/current Accrued Liability) falls below 80%

• Additional contribution approximately $50 million for each 1% Funded Ratio is less than 80%

• 2014 change in assumptions more conservative (realistic?) estimate of plan’s cost:
  o Increased ARC rate from 35.1% to 38.2% of payroll
  o Increased UAL from $942 million to $1.021 billion
  o Decreased Funded Ratio from 82.2% to 81.0%

• Funded Ratio remained above 80% due to investment rate of return of 17.3% for FY 2014
• **IF** assumptions are met, actuary projects:
  - Scheduled City contribution rates will increase from 27% to approximately 38% of payroll after FY2026
  - Scheduled City contributions will be greater than the ARC beginning about FY2021
  - The ARC rate will decrease to about 18% over the next 20 years
  - The Funded Ratio will remain above 80%
  - Plan will be funded on financially sound basis

• **BUT** Funded Ratio will fall below 80% and trigger additional contribution for FY2017 **IF** 0% rate of return for FY2015

• FY2015 year to date rates of return for all three city plans now at 0% +/- 2% points
GASB 68 Implementation

- City must comply with GASB 68 for FY2015.

- Financial reporting under GASB 68 bears no relationship to funding policy or contributions.

- Major changes for measuring and reporting pension liability are:
  - A single actuarial method for calculating the liability is mandated
  - The liability is reported directly on the balance sheet

- If in effect for FY2014 pension liability on the City’s balance sheet would have been $3.896 billion:
  - HPOPS – $1.651 billion
  - HFRRF – $0.343 billion
  - HMEPS – $1.902 billion

- Required use of market value of assets to offset the Accrued Liability:
  - Expected to create more volatility in the reported pension liability amounts
  - The initial liability for FY2015 expected to be significantly larger than the estimated preliminary amounts for FY2014 due to probability of poor investment returns for year 7
Increasing General Fund Pension Expenditures are Crowding Out Headcount/Services ($ in Thousands)

|            | FY2017 | FY2018 | FY2019 | FY2020 | FY2021 | FY2022 | FY2023 | FY2024 | FY2025 | FY2026 | FY2027 | FY2028 | FY2029 | FY2030 | FY2031 | FY2032 | FY2033 | FY2034 | FY2035 | FY2036 | FY2037 | FY2038 | FY2039 |
|------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| Fire - Classified | $20,175 | $21,884 | $23,220 | $24,093 | $24,076 | $27,979 | $27,772 | $28,325 | $32,699 | $48,738 | $51,984 | $53,981 | $70,506 | $74,299 | $76,352 | $81,204 | $82,141 | $83,719 | $90,248 | $92,380 | $92,789 | $92,807 |
| Municipal - Civilian | $18,660 | $19,610 | $20,317 | $23,675 | $25,253 | $24,812 | $23,524 | $20,317 | $34,437 | $48,738 | $51,984 | $53,981 | $37,994 | $41,537 | $41,204 | $61,204 | $62,141 | $63,719 | $92,458 | $92,380 | $92,789 | $92,807 |
| Total       | $68,566 | $72,139 | $74,075 | $78,319 | $80,944 | $105,342 | $105,045 | $106,528 | $94,165 | $133,936 | $135,513 | $151,886 | $175,995 | $186,985 | $195,423 | $185,567 | $190,886 | $216,307 | $265,307 | $308,108 | $331,695 | $322,059 |

% Growth

- Police - Classified: 2.29%
- Fire - Classified: 5.21%
- Municipal - Civilian: 2.68%
- Total: 5.73%

- FY2016 includes possible $25 Million HPOPS Payment; potential payments that would be required if HPOPS funding level falls below 80% are not included.
Effect of benefit changes on future plan costs

- In the LONG TERM benefit changes at HPOPS and HMEPS will reduce plan costs and ease budget stress.

- But in the short to intermediate term, the cost of the legacy benefits at HPOPS and HMEPS will continue to place significant stress on the budget.

- Without any change at HFRRF:
  - The cost of HFRRF benefits will continue to cause budget stress in the long term, and
  - Will result in significant disparity in benefit levels versus other city employees.

<table>
<thead>
<tr>
<th>Illustration of Future Retirement Benefits for City Employees Upon Retirement With 30 Years of Service</th>
<th>HFRRF (i)</th>
<th>HPOPS (ii)</th>
<th>SS (iv)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Initial annuity as a % of pre-retirement salary</td>
<td>91%</td>
<td>75%</td>
<td>50%+SS</td>
</tr>
<tr>
<td>2. Estimated additional lump sum from DROP</td>
<td>$750,000</td>
<td>none</td>
<td>none</td>
</tr>
<tr>
<td>3. Future automatic cost of living adjustments</td>
<td>yes</td>
<td>yes</td>
<td>no (iv)</td>
</tr>
<tr>
<td>4. Employee contribution rate (% of pay)</td>
<td>9.00%</td>
<td>10.25%</td>
<td>6.20%</td>
</tr>
<tr>
<td>5. Minimum age eligible for unreduced benefit</td>
<td>none</td>
<td>55</td>
<td>62</td>
</tr>
<tr>
<td>6. Overtime included in pay for pension purposes</td>
<td>yes</td>
<td>no</td>
<td>no</td>
</tr>
</tbody>
</table>

(i) Assuming no change in current benefits - % in item 1 from the 2014 CAFR
(ii) Applies to actives hired after 10/9/2004 - 36.9% of current actives
(iii) Applies to actives hired after 1/1/2008 - 33.4% of current actives
(iv) Social Security benefits have cost of living adjustments based on CPI
Finance Department

Questions?