

Draft Testimony

Texas House Committee Pensions, Investments & Financial Services

March 29, 2023

Good [morning]. I'm [Melissa Dubowski, Deputy Director at the Finance Department] and here this morning representing the City of Houston. Thank you for your time.

Firstly, on behalf of the City of Houston I want to again thank the members of this committee for hearing our testimony today. We also want to reiterate our gratitude for the support and leadership provided by the legislature during the 85th session on the implementation of Houston's pension reform. Many of the members of this committee helped to pass SB 2190 at that time, which solidified the reforms and put both the City and the pension systems on firm financial footing. Not only were the reforms memorialized in that bill critical to the City's fiscal health, but the reforms were also critical in securing a pension for the hardworking employees and retirees of the City. That legislation ended decades of "kicking the can down the road."

Reform's effect on net pension liability

The historic Pension Reform reduced the City's NPL in half (from \$8.21B to \$4.03B) in FY18. Even with volatile markets the past few years, the NPL in FY22 stood at just \$2.19B.

Funded Ratio

The Funded Ratios have consistently improved since the reform. The funded ratio has kept steady and even increased in FY22. This is partially due to the carryover from exceptionally great returns from previous fiscal year (FY21) and consistent contributions from the City—largely due to the corridor mechanism built into pension reforms—bolstering the funded status of the plans. Pre-reform, Fire's funded ratio was 80% compared to 95% today. Police's was 78% compared to 88% today.

Timing

But, there is still further progress to be made before consideration should be given to enhancing benefits. State Statute already has provisions in place that would allow the City and the plans to work together on a sustainable and affordable enhancement of benefits, **but only once the plans were fully funded**—reaching a

level of 100% funded. Increasing benefits now would jeopardize the gains that SB2190 solidified.

Cost of Proposed Legislation

You may hear from those testifying in favor of the bill that the proposed changes would come at no cost. Quite simply, that is not true. The “cost corridor” mechanism currently in statute, established the upper and lower bounds for the City’s contribution rate for the next 30 years. This mechanism has resulted in the City not only contributing the full Actuarially Determined Contribution, but actually contributing above that amount. Those excess contributions have resulted in paying down the unfunded liability at a faster rate. For example, in FY23 the ADC for Fire was 22.55% of pay, and the City is contributing 26.89%, resulting in an additional \$11.4M. For Police, the ADC was 27.02% of pay and the City is contributing 31.98%, resulting in an additional \$26M. Any enhanced benefits would increase the liability and cut into the acceleration of paying down the unfunded and potentially delay the pension systems reaching 100% funded status.

Rating agencies

Credit rating agencies have taken notice of these historic reforms. Mostly recently Moody's affirmed the City's GO rating (Aa3) citing the importance of the reforms on Houston's financial health.

Pending litigation

All litigation related to the 2017 reform package has been concluded. Most recently the Texas Supreme Court denied a petition for review by the Houston Firefighters' Relief and Retirement Fund (HFRRF) in its second lawsuit challenging the historic pension reform championed by Mayor Sylvester Turner.

Conclusion

The City's pension plans are more well-funded than they were pre-reform, ensuring that a pension check will be there to support our retirees that have dedicated their careers to serving Houstonians. Any enrichments could jeopardize the financial health of the plans, particularly given the current volatility of the markets and their effect on returns. Given that volatility, we would respectfully request that the statute remain unchanged—allowing the reforms to continue to work until such time that the plans reach a funded status of 100%. Only at that time, would it be fiscally prudent for the plans and the City to work together at the

local level and bring forward to this body a package of affordable and sustainable enhancements.

Thank you for your time and the opportunity share the City of Houston's perspective on this bill.