Comments on Texas House Bill 3340

Prepared for: House Committee on Pensions, Investments and Financial Services
Texas House of Representatives

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Chairman Capriglione and members of the committee:

Thank you for the opportunity to offer comments on Texas House Bill 3340 (HB3340) and the need for a proper actuarial analysis on the proposed changes to Houston fire and police pension benefits.

In 2017, policymakers took on a major effort to reform Houston's underfunded and increasingly costly police and firefighter retirement funds. Ultimately, stakeholders achieved a resolution allowing the city to continue to provide pension benefits to its workers while managing the runaway costs that had plagued their budgets in the previous years. These reforms significantly improved the pension system's funding, putting the city in a much more stable and manageable fiscal position.

The proposed pension benefit increases in HB 3340 would roll back the delicate balance between cost and risk that the city has achieved and could resummon the same funding challenges that existed up to 2017.

HB 3340 would adjust when a member of the plan is allowed to retire and begin drawing a full benefit, which would have a major actuarial impact on the current system and directly roll back the changes made in 2017 that set the fund up to have its current funding success.

Major pension benefit changes like this would significantly increase annual costs and demand serious long-term financial scrutiny to ensure that hard-won gains in solvency are not lost. To fully understand the impact of the changes proposed in the bill, policymakers need a full, 30-year actuarial analysis examining the cost implications on local property taxpayers using an array of different economic and market stress scenarios reflecting the types of real-world market volatility we've all experienced several times since 2000.

To date, HB 3340 has not been evaluated by an independent actuary to discern potentials costs and risk exposure, nor have the proposed changes been stress tested to account for future market volatility and lower-than-expected investment returns. Both the static cost projections of the enhancements if all actuarial assumptions prove true each year and the quantifiable risk associated with missing those actuarial assumptions are crucial to properly understanding the size and scope of rolling back the 2017 reforms.

Since pension benefits are ironclad promises made to public workers, policymakers need to know what it may take to fulfill those promises in a wide range of situations, be they ideal or suboptimal. Before making a financial decision of this magnitude, Texas lawmakers should require the level of scrutiny that other governments have applied for similar proposals.

Take, for example, a bill recently passed in Washington state for its police and fire pension system. That pension system has been overfunded, meaning it has more assets than what actuaries calculate is needed at the time, since its inception in the mid-1970s through prudent risk analysis and funding design. Due to decades of wise policies and work, the plan created a side account to pay (in full) for future benefit increases. The first benefit increase was passed last year: a multiplier increase.

Office of the State Actuary's fiscal note for that multiplier increase is an example of the level of detail that should be considered when adjusting a pension benefit. Washington state's thorough fiscal note included an analysis of:

- The 25-year costs to the employer (and taxpayers);
- Analysis of the pension system's funding trajectory going out 30 years;
- Stochastic modeling to assess how unexpected results under thousands of potential economic scenarios and outcomes would change costs and funding;
- Probability analysis on the likelihood that contributions will exceed current rates;
- And sensitivity analysis on the bill's projected effect on public workers' retirement rates.

Members of the legislature, especially those concerned with the cities in Texas potentially needed to increase property taxes on locals to pay for proposals like HB 3340, need to demand a similarly rigorous analysis so they can thoroughly evaluate the long term risks and costs to taxpayers associated with HB 3340 before adding more benefit promises to an already underfunded retirement system.

The 2017 pension reforms were a collaborative and informed effort involving many policymakers and stakeholders at both the local and state levels, and the product of that was a retirement infrastructure that properly balanced the needs of public safety workers, government employers, and taxpayers. State lawmakers employed a similar process in reforming the Texas Employees Retirement System (ERS), which is projected to save the state upwards of $16 billion over the next 30 years. To reap the benefits of these reforms, policymakers need to see them through and reject efforts to undermine them before they can achieve their long-term ends.

Unraveling the efforts from 2017 is likely to increase costs and risks to local property taxpayers and the city. The magnitude of these costs and risks are still unknown absent proper actuarial due diligence. Since Houston's pension system has not yet reached its destination of full funding—having the money to pay for benefits already promised to workers and retirees—unrolling the 2017 reform could interrupt the progress achieved to date on a complicated long-term reform.

Thank you again for the opportunity to submit technical comments on HB 3340. We are happy to answer any questions the committee may have.

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