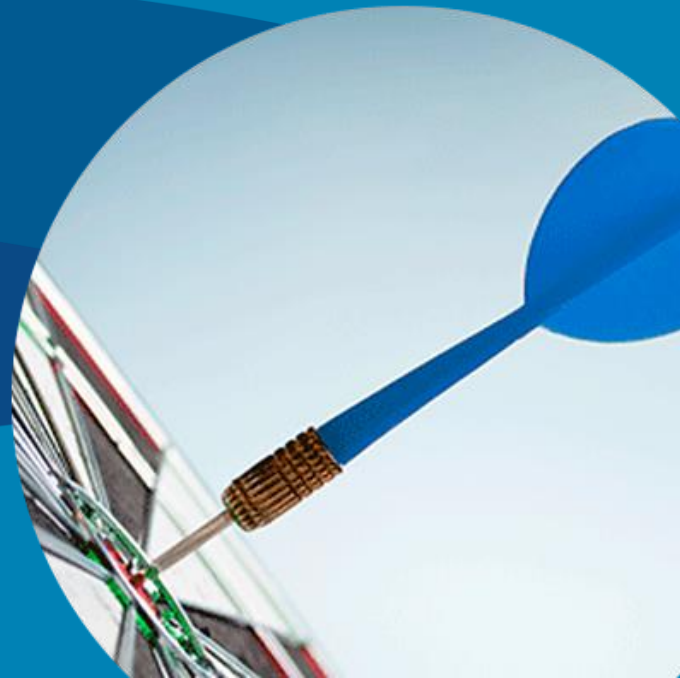


# 2022 Retirement Valuation Updates and Proposed Funding Strategy

City of Warwick, RI

Joe Newton

March 20, 2023



# Agenda

---

- Update on the pension programs
- Update on the post-retirement medical program
- Introduction of a comprehensive funding strategy for the City's retirement programs

# Post Retirement Benefits

---

- City currently manages the following programs
  - Municipal Employees Retirement Plan
  - Police/Fire I Pension Fund
  - Police II Pension Fund
  - Fire II Pension Fund
  - Post-Retirement Healthcare (All employees)

# 2022 Pension Actuarial Results: Funded Ratio

	2021 Valuation	2022 Valuation	Change
Municipal	76.4%	78.0%	1.6%
Fire II	82.8%	84.4%	1.6%
Police II	81.1%	81.6%	0.5%
Police/Fire I	<u>24.0%</u>	<u>24.0%</u>	<u>0.0%</u>
<b>Combined</b>	<b>61.5%</b>	<b>62.6%</b>	<b>1.1%</b>
<b>3 Open Plans Combined</b>	<b>79.9%</b>	<b>81.0%</b>	<b>1.1%</b>

Funded Ratio is the percentage of the current liability (accrued to date for services provided in the past) that is covered by current assets

80% is generally considered healthy, although all funding strategies should target 100%

# 2022 Pension Actuarial Results: UAAL

(\$ millions)

	2021 Valuation	2022 Valuation	Change
Municipal	\$47.6	\$44.9	-\$2.7
Fire II	\$22.1	\$21.7	-0.4
Police II	\$54.9	\$54.9	0.0
Police/Fire I	<u>\$232.4</u>	<u>\$231.5</u>	<u>-0.8</u>
<b>Combined</b>	<b>\$356.9</b>	<b>\$353.0</b>	<b>-\$3.9</b>
<b>3 Open Plans Combined</b>	\$124.5	\$121.4	-\$3.1

UAAL: Unfunded Actuarial Accrued Liability is the difference between the current liability and the current assets. There must be contributions to reduce this over time.

Want to see a decline each year.

# 2022 Pension Actuarial Results: City Contributions (\$ millions)

	2021 Valuation	2022 Valuation	Change
Fiscal Year contributions will occur	<u>2023</u>	<u>2024</u>	
Municipal	\$8.1	\$8.5	5.6%
Fire II	\$5.0	\$5.2	4.8%
Police II	\$5.7	\$5.9	3.6%
Police/Fire I	<u>\$20.6</u>	<u>\$21.7</u>	<u>5.5%</u>
<b>Combined</b>	<b>\$39.3</b>	<b>\$41.4</b>	<b>5.2%</b>
<b>Payroll</b>	\$52.0	\$54.4	4.5%
<b>Contribution as % of Payroll</b>	<b>75.6%</b>	<b>76.1%</b>	<b>+0.5%</b>
<b>3 Open Plans Combined</b>	\$18.7	\$19.6	4.8%
<b>Open Plan Contribution as % of Payroll</b>	<b>36.2%</b>	<b>36.3%</b>	<b>+0.1%</b>

# 2022 Actuarial Results: Retiree Medical Program

## \$ in millions

	2019 Valuation	2020 Valuation	2021 Valuation	2022 Valuation
Liability	\$363.2	\$383.3	\$405.6	\$397.4
Assets	<u>\$0.0</u>	<u>\$0.0</u>	<u>\$0.0</u>	<u>0.2</u>
UAAL	\$363.2	\$383.3	\$405.6	\$397.2
Funded Ratio	0%	0%	0%	0.1%

- The retiree medical program has not been actuarially (advanced) funded, but instead the annual premiums have been provided through the City's annual budget
- Generally, the annual change in the amounts has and is expected to grow faster than payroll and likely the City's budget

# Projected Retiree Medical Costs

## \$ in millions

	<b>Actual Cash Premiums for Retirees</b>	<b>Implicit Subsidies</b>	<b>Total Employer Provided Benefit</b>	<b>Annual Growth</b>
FY23	\$10.9	\$2.2	\$13.1	7.3%
FY24	\$11.7	\$2.4	\$14.0	8.0%
FY25	\$12.5	\$2.6	\$15.1	6.6%
FY26	\$13.4	\$2.7	\$16.1	5.4%
FY27	\$14.2	\$2.8	\$17.0	4.0%
FY28	\$14.8	\$2.9	\$17.7	3.6%
FY29	\$15.4	\$2.9	\$18.3	2.2%
FY30	\$16.0	\$2.8	\$18.7	3.2%



# Current Combined Projection (Employer Contributions Only)

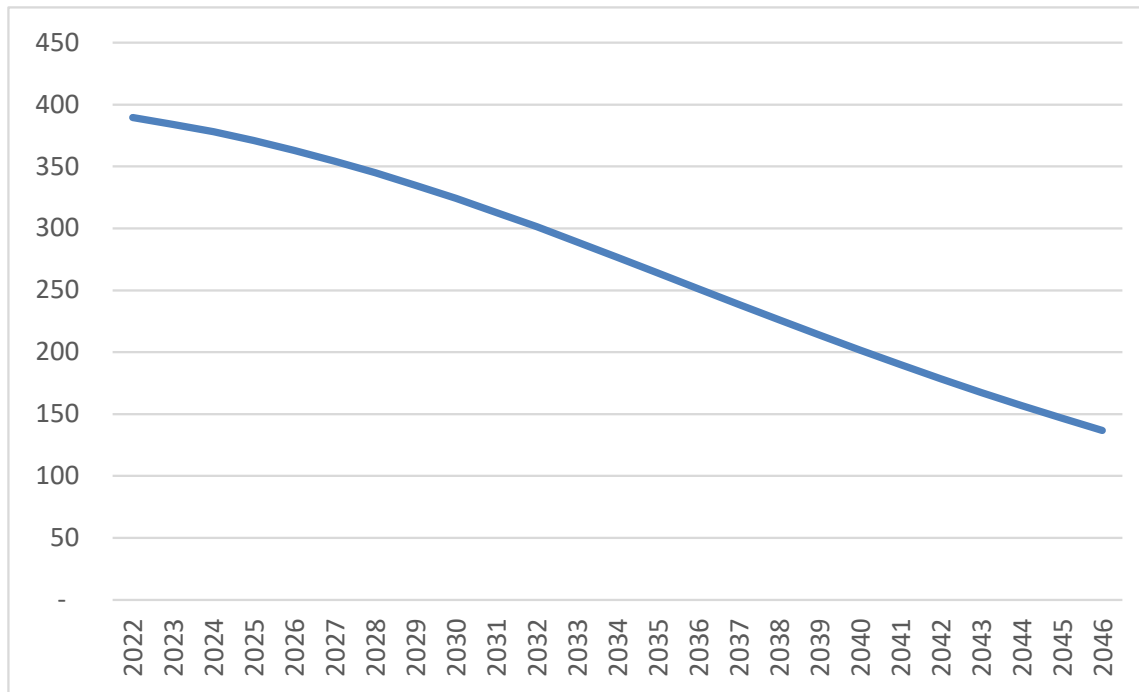
For Fiscal Year Ending June 30,	Municipal	Police II	Fire II	Police/ Fire I	OPEB Claims Payments	OPEB Trust Contribution	Total Employer Contribution	Annual Rate of Growth
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
2023	\$ 8.1	\$ 5.5	\$ 5.2	\$ 20.6	\$ 13.1	\$ -	\$ 52.4	
2024	8.5	5.9	5.2	21.7	14.0	-	55.4	5.7%
2025	8.7	6.2	5.3	22.6	15.1	-	57.9	4.5%
2026	8.9	6.3	5.3	23.5	16.1	-	60.1	3.9%
2027	3.6	6.4	5.4	24.4	17.0	-	56.8	-5.5%
2028	3.7	6.5	5.4	25.6	17.7	-	58.9	3.6%
2029	3.8	6.6	5.5	26.3	18.3	-	60.5	2.7%
2030	3.8	6.7	5.5	27.0	18.7	-	61.8	2.2%
2031	3.9	6.8	5.6	27.8	19.3	-	63.4	2.5%
2032	4.0	7.0	5.3	28.5	20.0	-	64.8	2.2%

\$ in millions

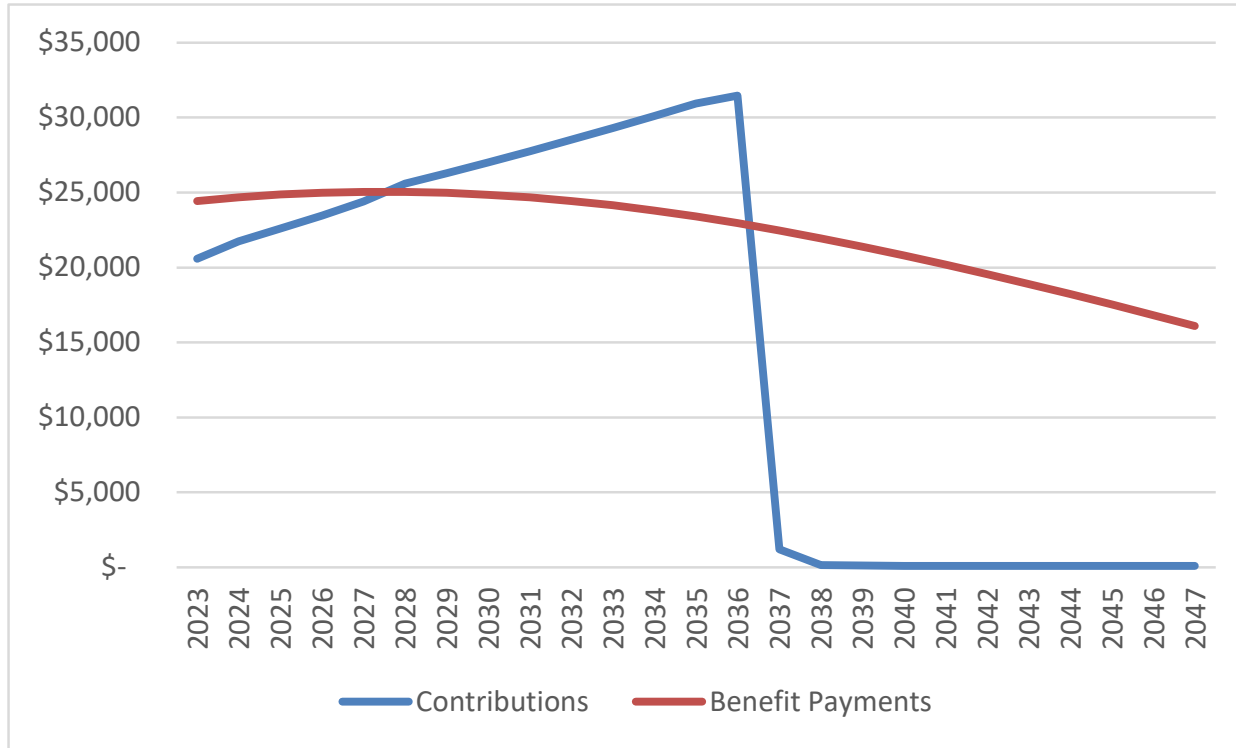
- If assumptions are met, the open pension plans should stabilize into a reasonable growth pattern.
- The Police/Fire 1 contribution will continue to grow
- The open plans have fixed amortization schedules that will complete in various years, which can lead to a meaningful drop in the contribution that year. The Municipal Plan in 2027 is an example.
- There have been some benefit changes to the retiree medical program that will dampen the growth for a while, but eventually be expected to return to annual growth rates above the rest of the City's budget.

# Police/Fire I: Projected Headcount

---



# Police/Fire I



The annual benefit payments will remain mostly flat as the annual COLAs are offset by mortality, and then eventually begin to decline

# Best option for new investment dollars?

	Police/Fire 1	Retiree Medical Program
Membership	All retirees, no new entrants	Open to new hires
Time horizon for new investments	~10 years	25+ years and ongoing
Annual Benefits (Outflows)	Steady, no longer growing, will begin to slowly decline	Volatile and growing
Reward if Investments Outperform	Slightly less contributions, assets locked up for decades	Meaningfully less contributions over the long term

# Police/Fire I: Alternative Funding Strategy

---

- The annual benefit payments are very predictable and stable, and not much different than current contributions
- We are proposing a modified pay-as-you-go strategy for this Fund.
- To determine annual City contributions, the valuation will split the liability into two parts:

	<b>Allocated Liability</b>	<b>Contribution Requirement</b>
Fully funded segment	Equal to the trust assets	Fully funded, so no need for further contributions
Non-funded segment	Remainder of liability	Contributions equal to the unfunded portion of the benefit payments

# Police/Fire I: Alternative Funding Strategy

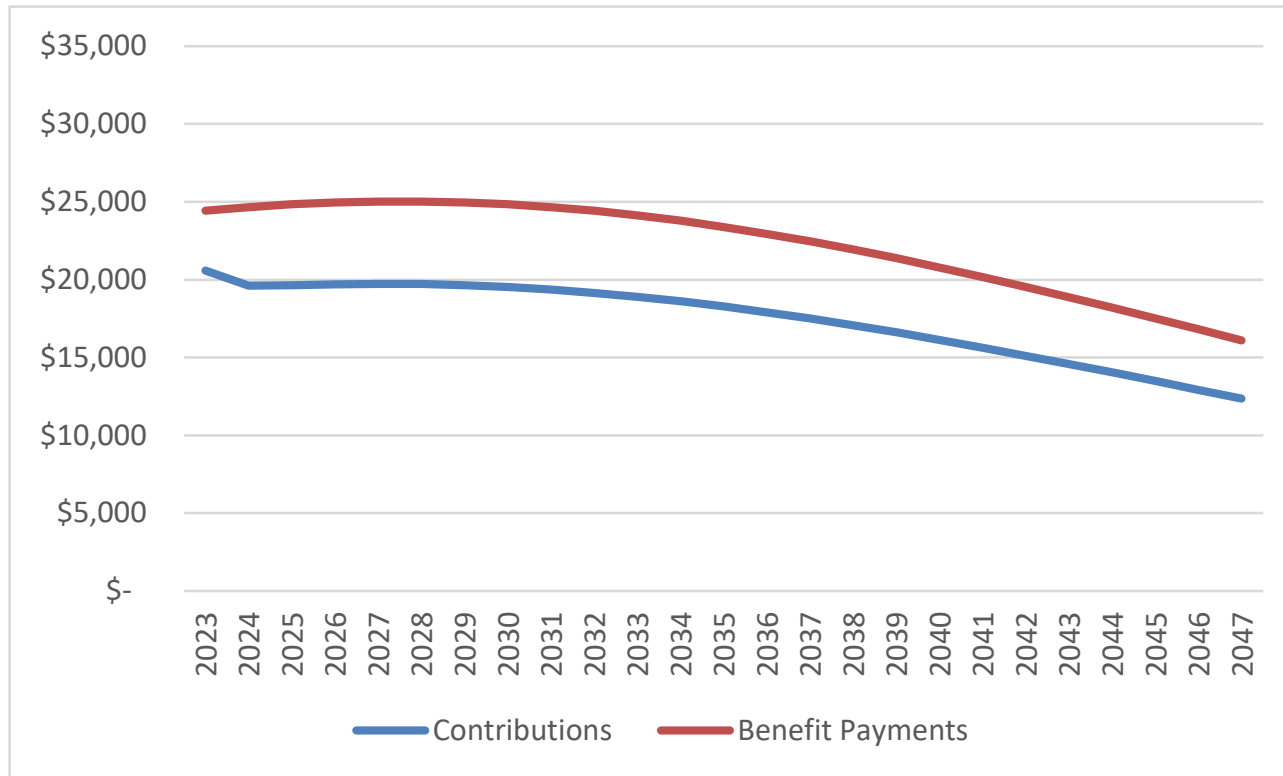
- Example Using FY22 results and projected FY24 benefits

	Total (A) + (B)	Fully funded Segment (A)	Non-funded Segment (B)
Liability	\$304.8m	\$73.3m	\$231.5m
Assets	<u>73.3m</u>	<u>73.3m</u>	<u>0.0m</u>
UAAL	\$231.5m	\$0.0m	\$231.5m
Funded Ratio	24.0%	100%	0%
FY24 Benefit Payments	\$24.7m	\$5.6m	\$19.1m
FY24 Contribution		\$0.0m	<b>\$19.1m</b>

- This compares to the \$21.7m required contribution from the current policy

# Police/Fire I: Alternative Funding Strategy

## Predictable, stable, and declining pattern



# Optimizing City Investment Dollars

---

- It would not be seen favorably by bond raters/debt issuers, or be financially prudent, to just reduce the advance funding towards the PF1 plan and not invest the difference against other long term obligations
- The retiree medical program would be much more sustainable if it were advance funded like the open pension plans, with investment earnings used to help finance future benefits
  - But it would take a significant increase in contributions to do that immediately
    - About \$12m more per year
  - The OPEB benefits cost about 8% of salary for new members if advance funded throughout their career
- This proposed strategy will:
  - begin the process of accumulating investment dollars for the retiree medical plan
  - provide a path to eventually meet the full actuarial funding requirement
  - provide stability in the annual City budget



# Full Strategy

---

- Move to a pay-as-you-go approach for Police/Fire I as described
- Keep current strategies for the other open pension Plans
- Set FY23 as a baseline pooled contribution amount to all retirement programs (\$52.4m)
- Set a annual growth rate that the City can sustain (2.50% per year, for example)
- Use that growth rate to determine a total amount to be contributed across all the programs
  - $\$52.4\text{m} * 1.025 = \$53.7\text{m}$  for FY24
- Then:
  - make all the required contributions into the individual programs
  - any balance left over flows into the OPEB trust

# Modified Projection on Comprehensive Funding Strategy using 2.50% annual growth

For Fiscal Year Ending June 30,	Municipal	Police II	Fire II	Police/ Fire I	OPEB Claims Payments	OPEB Trust Contribution	Total Employer Contribution	Annual Rate of Growth
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	No Change	No Change	No Change	Modified Paygo	No Change	Balance	2.50% Annual Growth	
2023	\$ 8.1	\$ 5.5	\$ 5.2	\$ 20.6	\$ 13.1	\$ -	\$ 52.4	
2024	8.5	5.9	5.2	19.1	14.0	1.0	53.7	2.5%
2025	8.7	6.2	5.3	19.1	15.1	0.7	55.1	2.5%
2026	8.9	6.3	5.3	19.1	16.1	0.7	56.4	2.5%
2027	3.6	6.4	5.4	19.1	17.0	6.3	57.9	2.5%
2028	3.7	6.5	5.4	19.1	17.7	6.9	59.3	2.5%
2029	3.8	6.6	5.5	19.0	18.3	7.6	60.8	2.5%
2030	3.8	6.7	5.5	18.9	18.8	8.6	62.3	2.5%
2031	3.9	6.8	5.6	18.8	19.4	9.4	63.9	2.5%
2032	4.0	7.0	5.3	18.6	20.1	10.6	65.5	2.5%

\$ in millions

- Item 8 is determined first, then the required contributions into Items 2-6 are paid, and any remaining balance is put into Item 7
- New investment monies that would have gone into PF1 and monies freed up when amortization bases in the other plans complete (see Municipal in 2027) are funneled into the OPEB trust
- This would be expected to accumulate \$65m in contributions into the OPEB trust over the next decade (even without accounting for investment earnings or other possible sources of funding)
- This also provides stability and predictability in the City's budget (2.5% annual growth)
- The risk of having more than 2.50% growth is the highest in the first few years where the balancing amount is about \$1m. But after 2027 there is a high probability of 2.50% annual growth until all programs are fully funded (UAAL reduced to \$0)

# OPEB Trust

---

- Other sources of funds could also be utilized to accumulate assets faster and as seed money to better position the Trust for success
  - Success means eventually pulling more money out of the Trust each year than putting in so that investment earnings help pay the benefits
- Possible monies for OPEB Trust contributions:
  - Investment dollars from PF1 funding strategy
  - Amortization cliffs from other plans
  - Seed money from other sources
  - Transfers from insurance reserves
  - Member contributions

# Projected OPEB Trust Results:

## All assumptions met and proposed funding strategy

For Fiscal Year Ending June 30,	Assets	Liabilities	UAAL	Funded Ratio	OPEB Claims Payments	OPEB Employer Contribution	OPEB Member Contribution	Total OPEB Contribution	Actuarially Determined Contribution
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
2023	\$ 5.2	\$ 264.8	\$ 259.5	2%	\$ 13.1	\$ 5.0	\$ -	\$ 18.1	\$ 24.4
2024	6.6	274.4	267.8	2%	14.0	1.0	-	15.0	24.9
2025	7.8	283.6	275.8	3%	15.1	0.7	-	15.8	25.6
2026	10.2	292.6	282.4	3%	16.1	0.7	1.2	18.0	26.3
2027	18.7	301.5	282.8	6%	17.0	6.3	1.2	24.5	27.0
2028	28.4	310.5	282.1	9%	17.7	6.9	1.2	25.8	27.2
2029	39.5	319.5	280.1	12%	18.3	7.6	1.3	27.2	27.3
2030	52.4	329.0	276.7	16%	18.8	8.6	1.3	28.6	27.3
2031	67.1	338.8	271.6	20%	19.4	9.4	1.3	30.1	27.3
2032	84.1	348.6	264.5	24%	20.1	10.6	1.4	32.0	27.1

\$ in millions

OPEB Trust projects to be fully funded in 23-26 years

Scenario:

2.50% annual pooled contribution growth rate

\$5m dollar initial City contributions from insurance reserves

Members begin contributing 2% of salary in 2026

6.9% annual investment returns for all plans

# Stress Test on Overall Projection: 5.9% Future Investment Returns for All Plans

For Fiscal Year Ending June 30,	Municipal	Police II	Fire II	Police/ Fire I	OPEB Claims Payments	OPEB Trust Contribution	Total Employer Contribution	Annual Rate of Growth
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
	No Change	No Change	No Change	Modified Paygo	No Change	Balance	2.50% Annual Growth	
2023	\$ 8.1	\$ 5.5	\$ 5.2	\$ 20.6	\$ 13.1	\$ -	\$ 52.4	
2024	8.5	5.9	5.2	19.1	14.0	1.0	53.7	2.5%
2025	9.1	6.6	5.4	19.3	15.1	-	55.5	3.2%
2026	9.6	7.1	5.7	19.5	16.1	-	58.0	4.6%
2027	4.7	7.6	6.0	19.8	17.0	4.5	59.5	2.5%
2028	5.1	8.1	6.2	20.0	17.7	3.8	61.0	2.5%
2029	5.4	8.4	6.4	20.0	18.3	4.0	62.5	2.5%
2030	5.6	8.7	6.5	19.9	18.8	4.5	64.1	2.5%
2031	5.9	9.0	6.7	19.8	19.4	4.8	65.7	2.5%
2032	6.2	9.4	6.6	19.7	20.1	5.5	67.3	2.5%
2033	6.4	9.7	6.7	19.5	20.5	6.1	69.0	2.5%
2034	6.7	10.1	6.9	19.3	21.1	6.7	70.7	2.5%
2035	7.0	10.4	7.1	19.0	21.8	7.1	72.5	2.5%
2036	7.4	10.8	7.3	18.7	22.2	7.9	74.3	2.5%
2037	7.6	11.1	7.5	18.3	22.7	9.0	76.1	2.5%

\$ in millions

OPEB Trust fully funded within 30 years in this scenario, all other open plans 85%-88% funded ratio long term

# Impact on City's Balance Sheet

- By dedicating meaningful funding to the OPEB Trust and some up front seed money (\$5m would be enough), the Trust would be able to immediately use the assumed investment return as the discount rate for determining the balance sheet liability for the OPEB plan. Example using 6.9% assumed return for the OPEB plan:

Municipal	Police II	Fire II	Police/ Fire I	OPEB Plan	Total Balance Sheet
(1)	(2)	(3)	(4)	(5)	(6)

## Net Pension and OPEB Liability (Balance Sheet Impact)

\$ in millions

Current	\$ 57.4	\$ 76.5	\$ 32.0	\$ 238.4	\$ 397.2	\$ 801.5
Proposed	57.4	76.5	32.0	238.4	255.0	659.3
	-	-	-	-	\$ (142.2)	\$ (142.2)

## Discount Rate

Current	6.90%	6.90%	6.90%	6.90%	3.69%
Proposed	6.90%	6.90%	6.90%	6.90%	6.90%

# Summary

---

- Decrease City's long term cost by generating more investment earnings to help pay the benefits
  - For example, if all plans were fully funded now (UAAL reduced to \$0) the total City FY24 contribution would be approximately \$15m
  - This proposal would be expected to eliminate all of UAAL for the open plans within 25 years
- Minimize annual budget risk by moving into a pooled pre-determined annual growth rate (2.5% per year)
- Generates approximate \$1.7m savings on FY24 budget
- Positive impact on financial statements and balance sheet, likely seen favorable by bond rating agencies
- Does this without reducing benefits or putting them at greater risk