

# City of Chandler

## Pension Funding Policy

### Public Safety Personnel Retirement System and Arizona State Retirement System

The intent of this policy is to clearly communicate the Council's pension funding objectives, its commitment to our employees and the sound financial management of the City, and to comply with new statutory requirements of Laws 2018, Chapter 112, including reviewing and adopting this policy annually.

The Government Finance Officers Association (GFOA) recommends the adoption of a pension funding policy that address three core elements:

- Actuarial Cost Method – The technique used to allocate the total present value of future benefits over an employee's working career (normal cost/service cost).
- Asset Smoothing Method – The technique used to recognize gains or losses in pension assets over some period of time so as to reduce the effects of market volatility and stabilize contributions.
- Amortization Policy – The length of time and the structure selected for increasing or decreasing contributions to systematically eliminate any unfunded actuarial accrued liability or surplus.

In addition to the three core elements identified by the GFOA, this policy also addresses the Council's position on:

- Pension Funding Goal
- Funding Pension Cost

Several terms are used throughout this policy:

Unfunded Actuarial Accrued Liability (UAAL) – The difference between trust assets and the estimated future cost of pensions earned by employees. The UAAL reflects the difference between actual results (interest earnings, member mortality, disability rates, etc.) and the assumptions used in previous actuarial valuations.

Annual Required Contribution (ARC) – The annual amount required to pay into the pension funds, as determined through annual actuarial valuations. It is comprised of two primary components: normal pension cost (the estimated cost of pension benefits earned by employees in the current year) and amortization of UAAL (the cost needed to cover the unfunded portion of pensions earned by employees in previous years). The UAAL is collected over a period of time referred to as the amortization period. The ARC is a percentage of the current payroll.

Funded Ratio – The ratio of fund assets to actuarial accrued liability. The higher the ratio, the better funded the pension, with 100% representing fully funded.

Intergenerational Equity – Ensures that no generation is burdened by substantially more or less pension costs than past or future generations.

The City's police and fire employees who are regularly assigned hazardous duty participate in the Public Safety Personnel Retirement System (PSPRS). All other eligible employees are covered by the Arizona State Retirement System (ASRS).

#### Public Safety Personnel Retirement System (PSPRS)

PSPRS is administered as an agent multiple-employer pension plan. An agent multiple-employer plan has two main functions: 1) to comingle assets of all plans under its administration, thus achieving economy of scale for more cost efficient investments and investing those assets for the benefit of all members under its administration, and 2) to serve as the statewide uniform administrator for the distribution of benefits.

Under an agent multiple-employer plan, each agency participating in the plan has an individual trust fund reflecting that agencies' assets and liabilities. Under this plan, all contributions are deposited to and distributions are made from that trust fund's assets, each trust fund has its own funded ratio and contribution rate, and each trust fund has a unique annual actuarial valuation. The City of Chandler has two trust funds, one for police employees and one for fire employees.

The three core elements outlined by the GFOA guidance are addressed by the statewide PSPRS board and discussed in section G of the annual individual actuarial valuations, which can be found on the PSPRS website. <http://www.psprs.com/investments--financials/annual-reports>

Council formally accepts the assets, liabilities, and current funding ratio of the City's PSPRS trust funds for Tier 1 and Tier 2 members from the June 30, 2021 actuarial valuation, which are detailed below.

| Trust Fund                 | Assets        | Accrued Liability | Unfunded Actuarial<br>Accrued Liability | Funded<br>Ratio |
|----------------------------|---------------|-------------------|-----------------------------------------|-----------------|
| Chandler Police            | \$221,781,355 | \$324,546,688     | \$102,765,333                           | 68.3%           |
| Chandler Fire              | 143,186,145   | 194,333,203       | 51,147,058                              | 73.7%           |
| City of Chandler<br>Totals | \$364,967,500 | \$518,879,891     | \$153,912,391                           | 70.3%           |

#### PSPRS Funding Goal

Pensions that are less than fully funded place the cost of service provided in earlier periods (amortization of UAAL) on the current taxpayers. Fully funded pension plans are the best way to achieve taxpayer and member intergenerational equity. Most funds in PSPRS are significantly underfunded and fall well short of the goal of intergenerational equity.

The Council's PSPRS funding ratio goal is to achieve 100% (fully funded) no later than June 30, 2036, and to reduce the annual employer contribution. Council established this goal for the following reasons:

- The PSPRS trust funds represent only the City of Chandler's liability.
- The fluctuating cost of an UAAL causes strain on the City's budget, affecting our ability to maintain, enhance, or add new services in the future.
- A fully funded pension is the best way to achieve taxpayer and member intergenerational equity.

Council has taken the following actions to achieve this goal:

- The City chose the 20-year amortization period instead of the 30-year one-time option, did not defer the *Fields* case (paid the full employer contribution rate increase in one year versus spreading over 3 years), and did not take advantage of PSPRS's credit service model option related to the *Parker* case to apply toward future retirement payments when refunding excess employee contributions.
- The City pays the full estimated employer contribution at the beginning of the Fiscal Year versus paying the actual amount through bi-weekly payrolls, allowing PSPRS to invest at a higher rate thereby increasing the amount of interest applied towards the City's UAAL.
- The City maintains the ARC payment from operating revenues – Council is committed to maintaining the full ARC payment (normal cost and UAAL amortization) from operating funds. The estimated combined ARC for FY 2021-22 was \$19.6 million and FY 2022-23 is approximately \$19.9 million and will be able to be paid from operating funds without diminishing City services.
- The City will commit additional payments above the ARC to achieve reduced ARC payments in the future. This projected additional payment to lower long-term costs may be adjusted annually based on the updated UAAL, economic environment, and available General Fund one-time funds.
  - o Additional payments to date total \$74.5 million and include - \$2.5 million in FY 2016-17, \$5 million in FY 2017-18, \$5 million in FY 2018-19, \$25 million in FY 2019-20, \$15 million in FY 2020-21, and \$22 million in FY 2021-22.
  - o The additional payment planned in FY 2022-23 is \$50 million. The prior year's budget compared to actual expenditures and updated UAAL will be reviewed annually and the excess payment will be adjusted accordingly.

Based on these actions, the Council's current plan is to: achieve its goal of 100% funding well before June 30, 2036, make additional payments early to save ongoing costs in future years, all while meeting the timeline set forth by the PSPRS June 30, 2021, actuarial valuation. The pay-down plan will be reviewed annually.

#### Funding PSPRS Pension Cost

It is the Council's policy that funding of the ARC from operating revenues will be a priority during the annual budget process before other service enhancements are considered.

## Arizona State Retirement System (ASRS)

ASRS is administered as a cost-sharing multiple-employer pension plan. This means that all agencies statewide are part of the same trust which is administered by a single administrator. In this type of pension, the funded ratio and contribution rates are the same for all participating entities. The City of Chandler's proportionate share comprises less than 1% of the total system, and the system has a funded ratio of 71.5%.

The three core elements outlined by the GFOA guidance are addressed by the statewide ASRS board and discussed in appendix III of the annual actuarial valuation, which can be found on the ASRS website. <https://www.azasrs.gov/content/annual-reports>

### ASRS Funding Goal

Since the ASRS trust fund is comprised of all participating agencies, there is no ability for the City of Chandler to address or influence its individual funded ratio.

### Funding ASRS Pension Cost

It is the Council's policy that funding of the ARC from operating revenues will be a priority during the annual budget process before other service enhancements are considered.