



June 4, 2018

City # 00610

City Official
Town of Highland Park
4700 Drexel Drive
Highland Park, TX 75205-3109

Subject: 2019 Municipal Contribution Rate

Dear City Official:

Presented below are your city’s contribution requirements to the Texas Municipal Retirement System (TMRS) for Plan Year 2019 (Calendar Year 2019, PY2019) as determined by the December 31, 2017 actuarial valuation. The actuarially determined contribution rates for retirement benefits and Supplemental Death Benefits (SDB), if any, are based on your city’s plan provisions in effect as of April 1, 2018 and the actuarial assumptions and methods adopted by the TMRS Board. Effective January 1, 2019, your city’s monthly contribution rates will be:

	<u>Phase-in Rate</u>	<u>Full Rate</u>
Normal Cost	6.31%	6.31%
Prior Service	<u>(0.97%)</u>	<u>(0.90%)</u>
Total Retirement Rate	5.34%	5.41%
Supplemental Death Benefit	<u>0.00%</u>	<u>0.00%</u>
Total Combined Contribution	5.34%	5.41%

Full information on your contribution rate, including an explanation of changes and available rate stabilization techniques, is contained in the attached report. The Total Retirement Rate shown in the Full Rate column above represents the Actuarially Determined Employer Contribution (ADEC) for PY2019 based on current TMRS funding policy. **The Total Combined Contribution Rate shown in the Phase-in Rate column above represents the minimum required contribution rate to TMRS for PY2019.** The difference represents the portion of your Full Rate that is eligible to be phased in. **Your city must contribute at least the Phase-in Rate though TMRS highly recommends that each city contribute as much toward the Full Rate as possible.** Please note that if your city chooses to contribute at a rate below the 2019 Full Rate, the contribution shortfall will be reflected in your city’s Unfunded Actuarial Accrued Liability (UAAL) and contribution rate in subsequent years. Cities may also choose to contribute at a rate level above the Full Rate. In lieu of phasing in to the Full Rate, a one-time UAAL re-amortization option is available to certain cities that experienced a net contribution rate increase greater than 0.5% due to the 2015 actuarial changes. See the “Phase-in Rates” section for more information on the phase-in/re-amortization options.

IMPORTANT NOTE: The pension disclosure and financial statement information necessary to assist your city with the financial reporting requirements of the Governmental Accounting Standards Board (GASB) will be provided in a separate document available later this summer.



If you have questions about your rate or if you wish to evaluate potential changes in your TMRS plan, contact TMRS at 800-924-8677.

Sincerely,

A handwritten signature in purple ink that reads "Eric W. Davis". The signature is written in a cursive, flowing style.

Eric W. Davis
Deputy Executive Director

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Calculation of Contribution Requirements	Details the calculation of the Full Retirement Rate (TMRS Plan Year - ADEC), Minimum Required Phase-in Retirement Rate, and the Supplemental Death Rate, if applicable, for your city. A comparison to the 2016 actuarial valuation results is included.
Summary of Benefit Provisions	A summary of plan provisions for plan years 2017 and 2018.
Amortization Bases and Payments	Information on the amortization bases and payments for your city.
Historical and Projected Accumulation of the BAF Balance	This schedule provides your city with historical cash flows, interest credits and the year-end balance of its Benefit Accumulation Fund (BAF), as well as projected values for calendar/plan years 2018 and 2019.
Reconciliation of Full Retirement Rate from Prior Actuarial Valuation Report	A detailed reconciliation of changes in your city's Full Retirement Rate (ADEC) since the prior valuation.
Phase-in Rates	An explanation of "Phase-in" including a question and answer section on Phase-in contributions and how they might affect your city. Also included are details of the one-time re-amortization option available to certain cities in lieu of phase-in.

Rate Stabilization Techniques

Contribution rate stabilization has been, and continues to be, a long term strategic goal of the TMRS Board of Trustees. Over the past several years, the Board has approved many actuarial changes in an effort to minimize the short term volatility in contribution rates while maximizing the long term sustainability of the System. Even so, some individual cities continue to experience significant changes in their contribution rate from year to year. Under the current funding policy in which rates are actuarially determined each year, contribution rate stabilization has been fully optimized at the System level; therefore, any further rate stabilization will have to be achieved at the city level.

One of the strategic goals of the Board of Trustees is to “Educate employers about the rate stabilization tools that are available to them through the current Plan design.” The TMRS Act and a Board Rule allow a TMRS employer to make additional contributions above the required contribution rate, on a voluntary basis, to its TMRS Benefit Accumulation Fund (BAF) account. Additional contributions can be in the form of a lump sum payment or additional monthly payments and are not subject to the statutory maximum contribution rate limits that are applicable to some TMRS employers.

The most effective way for a city to stabilize its TMRS contribution rate is to determine, during the budget process, an affordable contribution rate that exceeds the required calculated contribution rate and continue to pay monthly at this level from year to year, even when the calculated contribution rate goes down. This is particularly true for cities with an Unfunded Actuarial Accrued Liability (UAAL). These additional monthly contributions at a predetermined fixed rate accomplish at least the following: provides the city with a stable contribution rate from year-to-year for budgeting purposes; directly reduces the UAAL; accelerates the years needed to attain full funding (i.e. pays off the UAAL quicker); produces cost savings over the long run; and provides a contribution rate cushion for future adverse plan experience. A city can also make one or more lump sum contributions during the year which has a similar impact on the plan’s funding status, but is less effective from a rate stabilization perspective.

For cities with an Overfunded Actuarial Accrued Liability (OAAL or surplus), their calculated contribution rate (not less than 0.00%) is determined by decreasing the normal cost rate by a rate equal to a 25 year open amortization of the surplus assets. The result is a required contribution less than the normal cost (the cost of the current year accruals for active employees). This not only produces contribution rate volatility, but pushes the city’s funded status back towards 100% by using the surplus assets to pay for the current year accruals. In order to dampen contribution rate volatility and to increase the likelihood of maintaining a funded ratio greater than 100%, TMRS encourages cities in a surplus position to consider paying the full normal cost rate (or as much as possible toward the full normal cost rate) until the funded ratio is at least 110%.

As noted above, additional contributions in the form of monthly payments or lump sum contributions are entirely voluntary. A city can always revert back to paying only the required calculated rate each

month if financial circumstances change during the year. There is no formal action that needs to be taken by a city to contribute at a higher level than the required monthly minimum. Additional monthly contributions may be made during the normal payroll reporting process by simply filling out line 2. A. of Form TMRS 3 with the increased employer contribution rate. Lump sum contributions should be reported separately from the regular payroll reporting process and submitted with Form TMRS 3ADD.

If your city would like to explore the impact of any of these rate stabilization techniques on your TMRS plan, please contact Leslee Hardy, Director of Actuarial Services, at lhardy@tmrs.com.

Executive Summary

Valuation as of TMRS Plan Year (PY) Ending	12/31/2017	12/31/2016
Membership as of the Valuation Date		
• Number of		
- Active members	118	121
- Retirees and beneficiaries	112	105
- Inactive members	<u>38</u>	<u>32</u>
- Total	268	258
• Prior year's payroll provided by TMRS	\$ 12,381,528	\$ 11,929,614
• Valuation Payroll	\$ 12,449,142	\$ 12,405,759
Benefit Accumulation Fund (BAF) Assets		
• Market BAF Balance	\$ 77,740,809	\$ 71,255,990
• BAF crediting rate for PY	13.05%	6.73%
• Interest credited on beginning BAF balance	\$ 9,296,335	\$ 4,635,900
• Municipal contributions	668,603	374,590
• Member contributions during year	866,707	835,073
• Benefit and refund payments	4,346,827	3,436,977
Actuarial Value of Assets (AVA)		
• Market BAF Balance	\$ 77,740,809	\$ 71,255,990
• Actuarial Value of Assets (AVA)	75,446,251	72,989,714
• AVA as a Percentage of BAF	97.0%	102.4%
• Return on AVA	7.22%	6.37%
Actuarial Information		
• Actuarial accrued liability (AAL)	\$ 73,613,685	\$ 71,505,794
• Actuarial value of assets (AVA)	75,446,251	72,989,714
• Unfunded actuarial accrued liability (UAAL)	(1,832,566)	(1,483,920)
• UAAL as % of pay	(14.8%)	(12.4%)
• Funded ratio (AVA/AAL)	102.5%	102.1%
• Employer normal cost	6.31%	6.27%
• Prior Service Rate	(0.90%)	(0.73%)
Contribution Rates for TMRS Plan Year (PY)		
• Member	2019 7.00%	2018 7.00%
• Full retirement rate (ADEC)	5.41%	5.54%
• Phase-in retirement rate (minimum)	5.34%	4.84%
• Supplemental Death rate	0.00%	0.00%
Total Employer Contribution Estimates for PY		
• Projected payroll	2019 \$ 12,822,616	2018 \$ 12,777,932
• Minimum Phase-in contribution rate	5.34%	4.84%
• Estimated employer contribution	\$ 684,728	\$ 618,452

Note: TMRS Plan Year coincides with Calendar Year

Results from prior year reflect the plan provisions used in the 12/31/2017 valuation report.

Calculation of Contribution Requirements

	From Valuation Report as of	
	<u>December 31, 2017</u>	<u>December 31, 2016</u>
1. Prior year's payroll reported to TMRS	\$ 12,381,528	\$ 11,929,614
2. Valuation payroll	12,449,142	12,405,759
3. Employer normal cost rate	6.31%	6.27%
4. Actuarial liabilities		
a. Active members	\$ 29,133,491	\$ 31,488,137
b. Inactive members	5,404,702	5,671,526
c. Annuitants	<u>39,075,492</u>	<u>34,346,131</u>
d. Total actuarial accrued liability	\$ 73,613,685	\$ 71,505,794
5. Actuarial value of assets	<u>75,446,251</u>	<u>72,989,714</u>
6. Unfunded actuarial accrued liability (UAAL) (4d - 5)	\$ (1,832,566)	\$ (1,483,920)
7. Funded ratio (5 / 4d)	102.5%	102.1%
8. Equivalent Single Amortization Period*	25.0 years	25.0 years
9. Assumed payroll growth rate	3.0%	3.0%
Contribution Rate for TMRS Plan Year:		
	2019	2018
10. Full retirement rate		
a. Normal cost	6.31%	6.27%
b. Prior service	<u>(0.90%)</u>	<u>(0.73%)</u>
c. Full retirement rate	5.41%	5.54%
11. Minimum phase-in retirement rate		
a. Full retirement rate (10c)	5.41%	5.54%
b. Less phase-in deferral	<u>(0.07%)</u>	<u>(0.70%)</u>
c. Minimum phase-in retirement rate	5.34%	4.84%
12. Supplemental Death rate	0.00%	0.00%
13. Combined contribution rates		
a. Combined full rate (10c + 12)	5.41%	5.54%
b. Combined phase-in rate (11c + 12)	5.34%	4.84%

* New Losses are laddered on 25-year period.

Summary of Benefit Provisions

The plan provisions are adopted by the governing body of the City, within the options available in the state statutes governing TMRS. Plan provisions for the City were as follows:

	Plan Year 2018	Plan Year 2017
Employee deposit rate	7%	7%
Matching ratio (city to employee)	2 to 1	2 to 1
Years required for vesting	5	5
Retirement Eligibility (Age /Service)	60/5, 0/20	60/5, 0/20
Updated Service Credit	0%	0%
Annuity Increase (to retirees)	0% of CPI	0% of CPI
Supplemental Death Benefit to Active Employees	No	No
Supplemental Death Benefit to Retirees	No	No

Amortization Bases and Payments

Year Established	Description	Years Remaining	Base	Payment
2017	2017 Overfunded Non-Ad Hoc	25	\$(1,832,566)	\$(112,525)
	Total		(1,832,566)	(112,525)

Historical and Projected Accumulation of the BAF Balance

Year Ending December 31, (1)	Payroll for the Year (2)	Effective Retirement Contribution Rate ^a (3)	Employer Contributions for the Year (4)	Member Contributions for the Year (5)	Benefit Payments (6)	External Cash Flow for the Year (7)	Interest Credit (8)	BAF Balance ^b (9)
		(4) / (2)				(4) + (5) + (6)		
2015	\$ 11,251,001	3.95%	\$ 444,414	\$ 787,570	\$ (4,781,270)	\$ (3,549,286)	\$ 43,074	\$ 68,847,405
2016	\$ 11,929,614	3.14%	\$ 374,590	\$ 835,073	\$ (3,436,977)	\$ (2,227,314)	\$ 4,635,900	\$ 71,255,990
2017	\$ 12,381,528	5.40%	\$ 668,603	\$ 866,707	\$ (4,346,827)	\$ (2,811,517)	\$ 9,296,335	\$ 77,740,809
2018	\$ 12,449,142	4.84%	\$ 602,538	\$ 871,440	\$ (4,344,989)	\$ (2,871,011)	\$ 5,247,505	\$ 80,117,302
2019	\$ 12,822,616	5.34%	\$ 684,728	\$ 897,583	\$ (4,560,767)	\$ (2,978,456)	\$ 5,407,918	\$ 82,546,764

a. Effective retirement contribution rate is the actual rate determined by dividing the employer contribution received by the payroll paid.

b. BAF Balance may not sum due to rounding.

Reconciliation of Full Retirement Rate from Prior Actuarial Valuation Report

Actuarial valuations are based on long-term assumptions, and actual results in a specific year can, and almost certainly will, differ as actual experience deviates from the assumptions. The following table provides a detailed breakdown of changes in the retirement portion of your city’s contribution rate. This analysis reconciles the change in the retirement portion (ADEC) of your city’s contribution rate from 2018 to 2019, but will not reflect any change in the cost of the Supplemental Death Benefit (SDB), if your city currently has this provision. (Any changes in the cost of the SDB are primarily due to the changes in the average age of your city’s employee group and/or the number of covered retirees.) Following the table below is a brief description of the common sources for deviation from the expected.

Change in Full Retirement Rate	
Full Rate from 12/31/2016 Valuation (PY 2018 Rate)	5.54 %
Benefit changes	0.00 %
Return on Actuarial Value of Assets	(0.16)
Contribution lag/phase in/fully amortized prior bases	0.00
Payroll growth	(0.02)
Normal cost	0.04
Liability growth	0.01
Total change	(0.13) %
Full Rate from 12/31/2017 Valuation (PY 2019 Rate)	5.41 %

Benefit Changes - Shows the increase or decrease in the contribution rate associated with any modifications made to the member city’s TMRS plan provisions. This will also include any changes to the amortization period adopted by ordinance.

Return on Actuarial Value of Assets (AVA) - Shows the change in the contribution rate associated with the return on the AVA being different than the assumed 6.75%. For the year ending December 31, 2017, the return on an AVA basis was 7.22%. The impact may show as 0.00% due to rounding.

Contribution Lag/Phase In/Fully Amortized Prior Bases - Shows the total increase or decrease in the contribution rate associated with the phase in of contributions and/or any additional contributions above the full rate. The effect of the “Contribution Lag” is also included here and refers to the time delay between the actuarial valuation date and the date the contribution rate becomes effective. For TMRS member cities, the “Contribution Lag” is one year (i.e., the Actuarial Valuation as of December 31, 2017 sets the rate effective for Calendar Year 2019). **The impact of the**

“Contribution Lag” is expected to become immaterial once a city is contributing the Full Rate and the Full Rate stabilizes.

If a city chooses to contribute the minimum phase-in contribution, the difference between the Full Rate and the Phase-in Rate will be reflected as an actuarial loss in the next valuation’s UAAL. This will increase the Full Rate for future valuations.

Cities should carefully consider whether to pay the minimum Phase-in Rate, the Full Rate, or a rate somewhere in between. If a city begins to contribute the Full Rate immediately, the actuarial valuation anticipates that the Full Rate will stabilize for the duration of the amortization period. However, if the minimum phase-in contribution schedule is utilized, the ultimate Full Rate would be expected to be higher than the current Full Rate. For more information on the impact of the phase-in, please refer to the “Phase-in Rates” section.

In addition, it shows the impact of the bases, if any, which became fully amortized as of this valuation since payments for those bases are no longer part of the calculation of the prior service rate.

Payroll Growth - Shows the increase or decrease in the contribution rate associated with higher or lower than expected growth in the member city’s overall payroll. The amortization payments were calculated assuming payroll grows at 3.0% per year. Overall payroll growth in excess of 3.0% will typically cause a decrease in the prior service rate.

Normal Cost - Shows the increase or decrease in the contribution rate associated with changes in the average normal cost rate for the individual city’s population. The normal cost rate for an employee is the contribution rate which, if applied to a member’s compensation throughout their period of anticipated covered service with the municipality, would be sufficient to meet all benefits payable on their behalf. The salary-weighted average of the individual rates is the total normal cost rate.

Liability Growth - Shows the increase or decrease in the contribution rate associated with larger or lower than expected growth in the member city’s overall plan liabilities. The most significant sources for variance will be individual salary increases compared to the assumption and turnover.

Phase-in Rates

Phase-in Policy

After the actuarial changes first reflected in the December 31, 2013 actuarial valuation, any city that experienced a contribution rate increase in excess of 0.5% due to the 2013 actuarial changes was given the option to phase in contributions 0.5% per year until the full retirement rate is reached. Subsequently, at the December 2015 meeting and based on the results of the 2015 experience study, the TMRS Board of Trustees approved a new set of actuarial assumptions to be first reflected in the December 31, 2015 actuarial valuation. At the same time, the Board also approved a phase-in policy to help manage the potential impact of the 2015 actuarial changes on contribution rates. Specifically, any city that experienced a net contribution rate increase in excess of 0.5% due to the 2015 actuarial changes is eligible to phase in 0.5% per year until the full retirement rate is reached. For this purpose, the net contribution rate increase is the contribution rate increase resulting solely from the 2015 change in actuarial assumptions adjusted by the contribution rate decrease attributable to experience gains, if any.

Your city is eligible for a contribution rate phase-in due to one or both of the phase-in options discussed above.

Re-Amortization Option

At the December 2015 meeting, the TMRS Board also approved, in lieu of phase-in, a one-time re-amortization option for those cities with underfunded plans that experienced a net contribution rate increase (defined above) in excess of 0.5% due to the 2015 actuarial changes. These cities have a one-time option to instruct TMRS to aggregate and re-amortize all individual non-ad hoc UAAL bases up to a maximum of 30 years to offset any net contribution rate increases back to the limit of 0.5%. The resulting single period amortization is rounded up to the next integer, not to exceed 30 years, in determining the final contribution rate. There is one year remaining for eligible cities to request the re-amortization option. A request for this one-time re-amortization option may be made in 2018 and will be applied prospectively for calendar year 2019. For more details regarding the re-amortization option and its availability for your city, please contact Leslee Hardy, TMRS Director of Actuarial Services, at lhardy@tmrs.com.

What rate should my city pay?

Your city must contribute at least the Phase-in Rate and should consider paying more than this amount.

Can my city contribute more than the Phase-in Rate?

You may contribute at any rate you choose, but you must contribute at least the Phase-in Rate. Your city may choose to pay (1) the Full Rate, (2) a rate between the Phase-in Rate and the Full Rate, or (3) a rate above the Full Rate. The TMRS Act was amended effective January 1, 2008 to allow cities to make additional contributions to TMRS.

What is the impact of paying the Phase-in Rate or a rate below the Full Rate?

Each year that the actual contribution rate is less than the Full Rate, the difference generates an actuarial loss in the following year's actuarial valuation, which must be amortized as part of the UAAL by an increase in the Prior Service Rate. All other things being equal, the Full Rate for each successive year of the phase-in period will reflect the cumulative increases in the Prior Service Rate from all prior years. Cities that pay the Phase-in Rate or any rate less than the Full Rate are also likely to see their funding ratio decline or increase at a slower rate each year.

What is the impact of contributions in excess of the Full Rate?

Contributions above the Full Rate will have the exact opposite effect on your city as described above for contributions less than the Full Rate. Specifically, the amortization of actuarial gains created by additional contributions will decrease the Full Rate (by a decrease in the Prior Service Rate) in the following year's actuarial valuation. Cities that make contributions in excess of the Full Rate should also see their funding ratios improve more rapidly.

Can my city pay the Full Rate this year and change to the Phase-in Rate in a later year?

Yes. For any year in which your city is eligible to phase in the full retirement rate, TMRS will send you a rate letter showing both the Phase-in Rate and the Full Rate. The Phase-in Rate will be the minimum rate you must pay. As mentioned earlier, a city should consider paying more than the Phase-in Rate.

If my city makes plan changes that increase the cost of our plan (benefit improvements), can we phase in those additional costs?

No. The contribution rate increase due to benefit improvements will not change the Phase-in Amount used in determining the Phase-in Rate. The Phase-in Rate will increase by the same amount as the Full Rate. The Phase-in Rate was intended to assist those cities that needed additional time to budget for the Full Rate. Any city making plan changes should consider paying the Full Rate.

If my city makes changes that decrease the cost of our plan (benefit reductions), will our Phase-in Rate be affected?

Yes. Reductions in the Full Rate because of a plan benefit reduction will change the amount being phased in and the Phase-in Rate beginning with the year the plan changes are effective. The portion of the amount being phased in and not yet recognized will be reduced by the decrease in the Full Rate. If the decrease in the Full Rate due to reductions in plan benefits exceeds the remaining phase-in balance, your required contribution rate will be the reduced Full Rate based on the new plan provisions.

If I make a plan change in 2018, will my 2019 contribution rate be recalculated?

Yes. 2019 contribution rates will be re-determined for cities that adopt changes in plan benefits before the end of calendar year 2018.