

## **Texas Municipal Retirement System Actuarial Funding Policy Effective January 1, 2026**

### ***Background***

The primary financial objective of the Texas Municipal Retirement System (“TMRS” or “System”) is to pre-fund the long-term costs of promised benefits to plan members and beneficiaries at an approximate level percent of payroll from year to year. As an agent multiple employer plan with over 940 participating municipalities (employers), administration of the System includes engaging the services of a consulting actuary to assist in establishing contribution rates that will accomplish these funding objectives. The purpose of this Actuarial Funding Policy is to document the current funding policy of TMRS effective January 1, 2026 (first applicable to the December 31, 2025 actuarial valuation and plan changes adopted in 2026) as established by Statute, Board Rule or Board resolution in consultation with the System’s consulting actuary. The individual participating employer contribution determined annually under this funding policy is called the actuarially determined employer contribution (ADEC) and serves as the basis for determining the Full Retirement Rate contribution under TMRS.

### ***Goals and Objectives***

The goals and objectives of this funding policy are to:

1. Outline the funding policy components used in calculating the annual ADEC for each participating employer;
2. Achieve long-term full funding (funded ratio of 100% or greater) of the cost of promised and/or anticipated benefits;
3. Allocate the costs of benefits in a reasonable and equitable manner which promotes the principle of intergenerational equity;
4. Manage and control contribution rate volatility to the extent reasonably possible, consistent with other funding policy goals; and
5. Support transparency and accountability to stakeholders of TMRS.

### ***Actuarially Determined Employer Contribution Funding Policy Components***

TMRS Act § 855.405 and § 855.406 require each TMRS participating employer to contribute a monthly amount equal to the normal cost contribution and prior service contribution, respectively, as determined annually by the System’s consulting actuary. The normal cost contribution rate and prior service cost contribution rate are determined by the following three key components of this funding policy which are approved by the Board based on the advice of the actuary:

1. ***Actuarial Cost Method*** – *The technique used to allocate the total present value of future benefits (PVFB) over an employee’s working career.*

The Entry Age Normal (EAN) cost method is used in determining the normal cost (the portion of the PVFB allocated to the year following the valuation date) and the actuarial accrued liability (the portion of the PVFB allocated to years of service prior to the valuation date) of each active member. The individual EAN normal cost rate is the contribution rate which, if applied to a member’s compensation throughout their anticipated covered service with the employer, 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. The total Actuarial Accrued Liability (AAL) is the sum of the individual AALs. The Unfunded Actuarial Accrued Liability (UAAL) reflects the difference between the AAL and the Actuarial (Smoothed) Value of Assets (AVA). The prior service contribution rate amortizes the UAAL over the applicable period for that city in accordance with the amortization policy described below. The funded ratio equals the ratio of the AVA to the AAL.

2. 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.*

The Actuarial Value of Assets (AVA) is based on the Market Value of Assets (MVA) with ten-year smoothing applied. This is accomplished by recognizing each year 10% of the difference between the MVA and the expected AVA, based upon the assumed rate of return. Offsetting unrecognized gains and losses are immediately recognized, with the shortest remaining bases recognized first, and the net remaining bases continuing to be recognized over their original ten-year timeframe. The AVA is further adjusted by 33% of any difference between the initial value and a 12% corridor around the MVA, if necessary. A System-wide calculation to determine the ratio of the smoothed value to the market value in aggregate will be performed and that ratio will then be applied to each employer's market value of assets in determining their individual actuarial (smoothed) value of assets.

3. Amortization Policy – *The length of time and the structure selected for increasing or decreasing contributions to systematically eliminate any Unfunded Actuarial Accrued Liability (UAAL) or surplus.*

TMRS Act § 855.110(c) allows the Board the authority, after consultation with their consulting actuary, by rule or by funding policy, to:

- establish separate open or closed amortization periods up to a maximum of 30 years for each participating employer;
- decrease or increase amortization periods, not to exceed 30 years; and
- set different amortization periods for UAALs arising from different types of events that generate liabilities, and to ladder the amortization of the liabilities.

The current Board adopted amortization policy is summarized below:

- a. For underfunded plans, the amortization is a level percentage of payroll over a closed period using the process of “laddering” which separately tracks different amortization components or bases.  
Each valuation, new losses and benefit increases are amortized over a maximum period of 20 years with that period reduced by 1 year for each active member less than 15. Previously created amortization bases will continue to be amortized on their original schedule as determined by prior funding policy.
- b. New gains, including lump sum contributions, are offset against and amortized over the same period as the current largest outstanding loss base for the specific employer which, in turn, reduces contribution rate volatility.
- c. For overfunded plans, all prior bases (ad hoc and non-ad hoc) are erased and one surplus base is established. The asset surplus is used to generate a contribution credit for the year that is projected to remain the same over all time horizons and keep the funded ratio constant year over year. This provides for adequate surplus management and reduces contribution rate volatility.

- d. Ad hoc benefit enhancements create a separate UAAL base or ladder and are amortized on a level dollar basis over individual closed periods equal to the minimum of 12 years or the remaining life expectancy of the group; however, if the non-ad hoc (level percent) amortization factor is smaller due to a shorter amortization period based on the employer's size, ad hoc enhancements will be amortized the same as any other loss.
- e. For plans closed to new members, a 20-year level dollar amortization schedule is applicable with the consulting actuary's discretion to use a lower period, if necessary or appropriate, to be re-evaluated annually. Employers may request an extended amortization period up to 30 years subject to Board approval in consultation with the actuary and annual re-evaluation. The new higher rate will become effective the same date that the plan is closed and any applicable phase-in contribution rate will be eliminated. Benefit enhancements granted after the plan closing date are subject to more stringent funding requirements. Such funding requirements are subject to Board approval.

### ***Actuarially Determined Employer Contribution Phase-in Policy***

TMRS Act § 855.407(h)(1) allows the Board to phase-in contribution rate increases in excess of 0.5% resulting from actuarial changes (including changes in assumptions and/or methods) over a reasonable period of time. TMRS Act § 855.407(i) states that employers eligible to phase-in contribution rate increases are not required to do so.

### ***Actuarial Assumptions for Actuarial Valuation and Funding Purposes***

TMRS Act § 855.205(c) requires that at least once every 5 years, the System's actuary perform an actuarial experience investigation study and make recommendations to the Board based on the results of the experience study. TMRS generally performs this investigation study every 4 years. The recommendations for actuarial assumptions to be used in the annual actuarial valuations are grouped into the following two major categories:

1. Economic assumptions – including investment return, individual salary increases, overall payroll growth, etc.
2. Demographic assumptions – including rates of termination, forfeiture, service retirement, disability retirement, mortality, etc.

Actuarial assumptions adopted by the Board for use in the actuarial valuation affect only the timing of contributions. The ultimate contribution level is determined by the benefits and expense actually paid offset by actual investment returns. To the extent that actual experience deviates from the assumptions, experience gains and losses will occur. These gains (or losses) then serve to decrease (or increase) the future contribution requirements.

The actuarial assumptions represent the Board's best estimate of anticipated experience under TMRS and are intended to be long term in nature. In developing the actuarial assumption set, the Board considers not only past experience, but also trends, external forces and future expectations.

### ***Repeating vs Ad hoc Benefits***

Under the TMRS Act, cities can provide Updated Service Credits (USC) and Cost of Living Adjustments (COLA) on (1) a repeating basis (which an ordinance from the City is not required

each year) or (2) an ad hoc basis (which requires the City to readopt the new enhancement by ordinance each time it is granted). If the City has elected a repeating option, the actuarial valuation and resulting contribution rates assume that level of benefits will be provided in perpetuity.

Each time a City adopts a new ad hoc benefit, the value of that one enhancement is amortized over a 12-year period per item (d) in the Amortization Policy section above.

However, if a City triggers the conditions below of providing ad hoc enhancements on a regular basis, the enhancements will be deemed Effectively Repeating and an assumption will be incorporated into the funding cost anticipating the pattern will continue.

Due to the retroactive catch-up features of TMRS benefits, a new ad hoc enhancement will trigger the Effectively Repeating conditions if the same type of enhancement had also been granted in one of the three previous years, making the current enhancement the second in four or fewer years.

With USC and/or COLA plan changes adopted beginning in 2026 (i.e., for USC and COLA benefits effective January 1, 2027 or after), each time the City triggers the condition to be deemed Effectively Repeating, in addition to the cost of the ad hoc enhancement being granted, a repeating assumption equal to 20% of the level of benefit granted will be added into the funding cost. Thus, once a City has triggered the condition 5 times, the full repeating cost of the enhancement would be reflected in the contribution rate.

Once triggered, an ad hoc City will have to go three years without granting the enhancement to have the Effectively Repeating assumption removed. The City may formally request the assumption be removed before the end of the three-year period, with the conditions that (1) they will not grant another ad hoc enhancement of the same type within three years from their last adoption and (2) if they do grant another ad hoc in the three-year period, their funding costs will be reflected as 100% Repeating.

For a City with Repeating benefits to have the Repeating assumption removed, they will have to remove the repeating enhancement by ordinance. If an ad hoc enhancement of the same type is granted that year or in any of the next two years, the full 100% Effectively Repeating assumption will be reflected in the City's funding cost. If the City does not adopt an Ad hoc enhancement within the three-year window, they will then fall under the 20% graded Effectively Repeating rules.

### ***Funding Policy History***

Actuarial Funding Policy Effective January 1, 2026, adopted October 2, 2025  
Actuarial Funding Policy Effective January 1, 2020 adopted December 5, 2019  
Actuarial Funding Policy Effective December 31, 2015 adopted February 18, 2016  
Actuarial Funding Policy Effective December 31, 2013 adopted October 24, 2014