



**MEMORANDUM**

**TO:** HONORABLE MAYOR &  
CITY COUNCIL

**FROM:** Scott P. Johnson

**SUBJECT:** Update on Plan of Finance  
to Issue Pension Obligation Bonds

**DATE:** April 23, 2012

City Administrator

Date

Approval

4/24/12

**INFORMATION**

The purpose of this informational report is to provide the Mayor and City Council with an update on the status of the plan of finance to issue Pension Obligation Bonds ("POB's") to prefund the City's contributions for the Police and Fire Retirement System ("PFRS") for a suspended period between five to seven years.

The City has assembled a financing team for the proposed issuance of the Taxable Pension Obligation Bonds Series 2012 (the "2012 POBs"), to fund a pre-payment amount estimated at \$225.5 million to the PFRS System in order to reduce the Unfunded Actuarial Accrued Liability (UAAL) of the System, improve the funded ratio, mitigate risk to the City's general fund and stabilize the funding for the benefit of the System's beneficiaries.

**PFRS Valuation Study as of July 1, 2011**

As illustrated in the chart below, based on the most recent PFRS actuarial valuation study as of July 1, 2011, (which will be presented by Bartell Associates, LLC (the Board's actuary), to the PFRS Board during their meeting on April 25, 2012), the Unfunded Actuarial Accrued Liability ("UAAL") is estimated to be \$426.8 million and the plan's funded ratio is estimated at 37.5%, compared to \$494.4 million and 37.6% respectively, as of July 1, 2010. The UAAL is the difference between the present value of projected benefits of the plan compared to the present value of plan assets. The funded ratio is calculated by dividing the Actuarial Value of Plan Assets over the Actuarial Value of Plan Liabilities.

After considering the Plan of Finance for the purpose of providing PFRS with an estimated prepayment contribution amount of approximately \$225.5 million, PFRS' UAAL will be reduced from \$426.8 million (as of July 1, 2011) to approximately \$201.3 million and the funded ratio will improve from 37.5% to an estimated ratio of 70.5%. Additionally, pre-funding some of the long-term liability will enable the fund to generate greater returns and will thereby further reduce the City's UAAL over the long-term.

## Estimated Funded Ratio

	July 1, 2011	July 1, 2011 with Prepayment Contribution
Estimated Prepayment Contribution	N/A	\$225,500,000
Estimated Actuarial Value of Plan Assets	256,394,000	481,894,000
Actuarial Liability	683,162,000	683,162,000
Unfunded Actuarial Liability	426,768,000	201,268,000
<b>Estimated Funded Ratio</b>	<b>37.5%</b>	<b>70.5%</b>

### Changes in Assumptions Result in Net Positive Reductions to UAAL

It should be noted that the City Administration worked with an independent consultant from First Southwest Company to provide an objective review of the assumptions which were recently presented to the Board for consideration as the Board reviewed the Actuary's draft experience study. Based on this input, the Board directed their actuary to work with the City and its consultant to review the actuarial data provided. The actuary's updated July 1, 2011 actuarial valuation, to be presented on April 25, 2012, includes assumption changes on salary increases that had a net positive impact on the UAAL which resulted in reducing the UAAL by \$50.2 million. In addition, other changes in assumptions such as the impact of MOU changes as the result of collective bargaining related to active public safety employees and staff's comprehensive updates to the data-base on spousal data resulted in further reductions to the UAAL by \$66 million. However, improvements in mortality rates (due to people living longer) and the Board's decision to reduce the discount rate from 7.0% to 6.75% resulted in increases to the UAAL by \$17.1 million and \$14.6 million respectively.

### The City's Annual PFRS Obligations

The City issued POB's in 1997 which provided a pre-payment for a suspended period from February 25, 1997 to June 30, 2011. Since July 2011, the City has made monthly payments of approximately \$3.8 million on a pay-as-you-go basis from the tax override funds for FY 2011-12 in accordance with the actuarial required contribution approved by the PFRS Board. The City is required to continue contributing to PFRS to fund the UAAL. Based on the most recent actuarial valuation, the annual contribution for fiscal year 2012-13 is estimated to be \$38.5 million.

In FY 2012-13, the City's total obligation for the PFRS unfunded liability (for the annual required contributions as well as bond debt service payments) will total approximately \$98.3 million. However, the projected available revenue (from the Annuity and the Tax Override) for PFRS obligation is only \$72.0 million; therefore, if the City does not move forward with issuing the proposed 2012 POB's, there will be an annual shortfall of approximately \$26.3 million. This shortfall and similarly larger shortfalls in future years will become the liability of the City's General Purpose Fund.

In return for the prefunding contribution and the resulting liability to be incurred from the proposed sale of the POB's, the City proposes to reduce the Recommended PFRS Contributions over the next five to seven years in a proportionate amount as shown below.

Fiscal Year Ending	Actuarial Recommended Contributions (ARC)	Proposed Prepayment
2013	\$46,500,000	\$225,500,000
2014	48,800,000	5,000,000
2015	50,800,000	5,000,000
2016	52,500,000	5,000,000
2017	55,000,000	5,000,000
2018	57,600,000	5,000,000

Based on the proposed POB's financing plan, in lieu of making the annual Actuarial Recommended Contributions (ARC), the City would make the initial prepayment contribution of \$225.5 million to PFRS in July, 2012. In addition, the proposed plan anticipates that the City will make annual payments from the tax override funds of \$5.0 million per year in subsequent years (fiscal year ending 2014 through 2018). Prior to the end of the pre-payment period, the City will evaluate options as to how the City will fund the PFRS System when it would otherwise resume annual contributions.

Following is a schedule of actions necessary by the Board and the City to complete the POB's financing by July 2012:

- City staff will be working with the PFRS Attorney on a funding agreement which will be presented to the PFRS Board on May 23<sup>rd</sup> for final authorization of the funding agreement.
- City staff will present an ordinance along with a report with detail information on the financing plan on May 8, 2012 to the Finance and Management Committee which will be forwarded for Council's approval on May 15, 2012 for the first reading of the ordinance seeking authorization for the issuance of the 2012 POBs.
- Staff will return to Council in June 2012 for the second reading of the ordinance and approval of a resolution for the issuance and sale of the 2012 POBs.

Respectfully submitted,

  
 SCOTT P. JOHNSON  
 Assistant City Administrator

For questions please contact Katano Kasaine, Treasury Manager, at (510) 238-2989.