LEGISLATIVE BUDGET BOARD
Austin, Texas

FISCAL NOTE, 85TH LEGISLATIVE REGULAR SESSION

May 23, 2017

TO: Honorable Dan Patrick, Lieutenant Governor, Senate
Honorable Joe Straus, Speaker of the House, House of Representatives

FROM: Ursula Parks, Director, Legislative Budget Board

IN RE: **SB2190** by Huffman (Relating to the public retirement systems of certain municipalities.), **Conference Committee Report**

No significant fiscal implication to the State is anticipated.

General Provisions

The bill would amend multiple sections of the Revised Statutes relating to the Houston Police, Firefighter, and Municipal Employee pension systems.

The bill would set requirements on the qualifications for the Municipal Fund actuary for all three funds.

The bill would require each pension to perform several reports and analyses. Every year each fund actuary and municipal actuary separately would produce a risk sharing valuation study (RSVS) and present the findings no later than 150 days after the end of the fiscal year. The bill requires the RSVS to calculate the unfunded actuarial accrued liability and estimate the municipal contribution rate.

The bill would set the process if the municipal and fund actuary contribution rate varies by more than two percent.

The bill would require the fund and municipality to separately perform an initial RSVS dated as of June 30, 2016 and project the corridor midpoint for 31 fiscal years beginning July 1, 2017.

The bill would require that at least once every four years the fund actuary conduct an Actuarial Experience Study (AES) no later than September 30. The AES would include all assumptions and methods recommended by the fund actuary and summaries of the reconciled actuarial data used in the creation of the AES.

The municipality as of the 2017 effective date would contribute at least biweekly to the funds an amount equal to the municipal contribution rate multiplied by the pensionable payroll for the biweekly period. The bill would require that the municipal contribution rate not exceed the maximum contribution rate or be less than the minimum contribution rate.

The initial RSVS would set the minimum and maximum contribution rate for the municipality, called the corridor midpoint. The bill provides authority and process to make changes to the system if the RSVS estimated municipal contribution is above or below the corridor midpoint. The fund must notify the PRB no later than 30 days after the fund changes the Municipal Contribution Rate when the rate would be outside the corridor midpoint.

The PRB shall notify the Governor, Lt. Governor, Speaker of the House, and legislative committees that have principal jurisdiction over pensions if the PRB determines the funds are not in compliance.

The bill would require once every three years the board of each pension system hire an independent investment consultant to produce a report that includes the pension's:

a) compliance with its investment policy statement,
b) asset allocation,
c) portfolio structure,
d) investment manager or advisor performance reviews,
e) benchmarks for each asset class,
f) evaluation of fees and trading costs,
g) evaluation of investment in any leverage, foreign exchange, or other hedging transactions,
h) and evaluations of investments-related disclosures in the annual reports or valuations.

Under provisions of the bill, a municipality may issue pension obligation bonds (POBs) to fund all or part of the unfunded liability only if the majority of voters approves the issuance at an election called for that purpose.

Provisions Relating to Firefighter Pension System

The board of the fund and the municipality may alter benefit types or amounts, the means of determining contribution rates, or the contribution rates, but may not increase the assumed rate of return to be more than 7 percent per year, extend the amortization period of the liability greater than 30 years, or allow the municipality's contributions to be less than the minimum or greater than the maximum municipal contribution rate.

Limits the number of years a Deferred Retirement Option Plan (DROP) participant who has 20 years of service can participate to 10 years.

The active member's contribution rate changes from 8.35 percent of the member's salary to 10.5 percent after the year 2017 effective date.

Provisions Relating to the Police Pension System

The active member's monthly contribution rate changes from 8.75 percent to 10.5 percent of the participant's pay.

The maximum number of years an active member may participate in DROP is 20 years after the member receives the hypothetical earning rate.

The bill changes the members in military service from being entitled to being eligible for counting uniformed service towards years of service.

The board and municipality may not enter into an agreement to increase the assumed rate of return to be more than 7 percent per year, extend the amortization period of the liability greater than 30 years, or allow the municipality's contributions to be less than the minimum or greater than the maximum municipal contribution rate.

Provisions Relating to the Municipal Pension System

The bill would modify an employee's retirement grouping based on date of hire. The groupings are A, B, and D.

The bill would establish member contributions rate on or after the 2017 effective date, and the municipal contribution rate on or after July 1, 2018.

Group	2017 Effective Date	July, 1, 2018
A	7%	8%
B	2%	4%
D	2%	2%

On or after January 1, 2018 each group D member would contribute one percent of the member's biweekly salary to a notional account with an annual return rate no less than 2.5 percent and no higher than 7.5 percent.

The bill would modify the requirements for DROP participation by requiring members to meet normal retirement eligibility requirements unless the member met the eligibility requirements before January 1, 2005. Members who had five years of service before January 1, 2005 and the sum of the member's years of service and age in years was equal to or greater than 68 would also qualify for DROP.

The bill would require the board beginning January 1, 2018 to establish an interest rate for DROP accounts that is not less than 2.5 percent and not greater than 7.5 percent. A DROP participant would be required to pay contributions to the pension system for all the participant's time in DROP that would constitute service in order receive credit to the DROP account.

The bill would take effect July 1, 2017 if it receives a two-thirds vote in each chamber; otherwise, it would take effect September 1, 2017.

Local Government Impact

The City of Houston estimates the required contribution to the pension systems in fiscal year 2018 would be $704,556,462 without legislative changes and $408,141,348 with legislative changes and Pension Obligation Bonds (POBs) issued. The debt service in fiscal year 2018 for POBs would be $25,527,988.

Over a five year period the City of Houston estimates without reform the city would contribute $3.7 billion to the pension systems. With reform and issuances of POBs the city would contribute $2.0 billion. The estimated debt service would be $0.2 billion. The city projects a savings of $1.4 billion dollars over a five year period.

Source Agencies: 338 Pension Review Board

LBB Staff: UP, BM, AG, GG, BRi