PSPRS: What we know

I am not an expert in PSPRS. The following presentation represents attendance at two recent PSPRS presentations, as well as direct input from PSPRS.

What is PSPRS?

- A state pension system for Fire and Police
- Once an organization joins to you are state mandated to remain in the system
- Each agency has their own bucket of money so an unfunded liability is owned by that agency
- The plan is run by a board of directors appointed at the State level
- We receive a bill every year that we must pay

PSPRS Manages

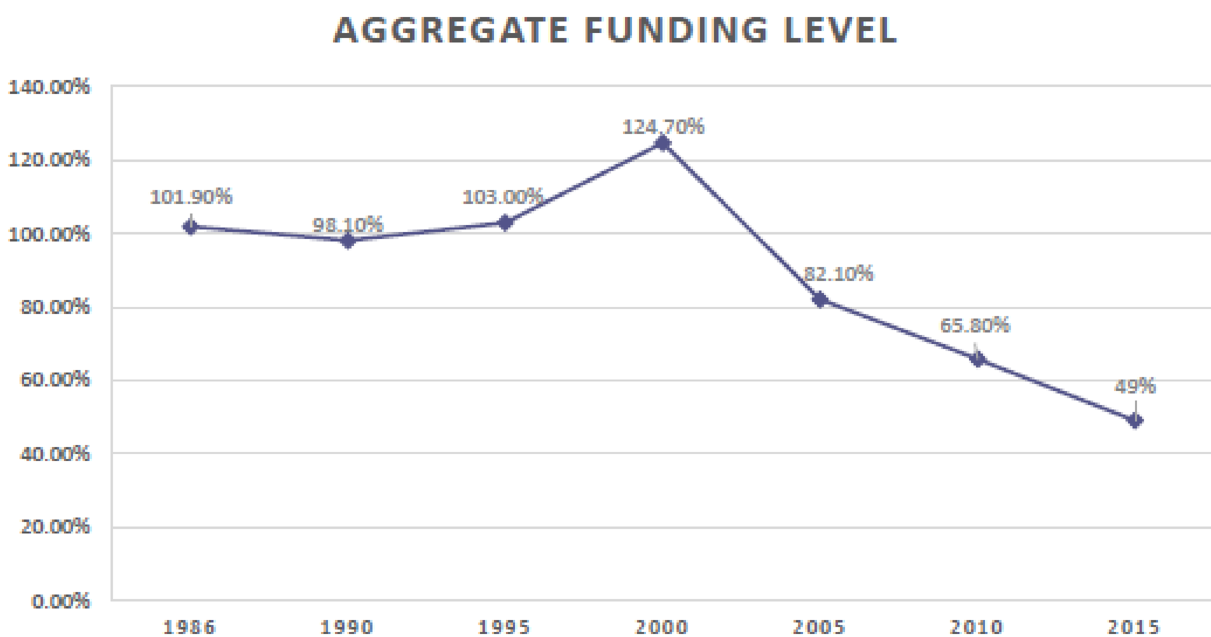
- What does PSPRS manage?
- $8.9 billion in assets for members:
- PSPRS (police, fire, other)
  - 33,390 total members in Tier 1, 2 and soon 3 employee tiers
- CORP (corrections officers)
  - 21,423 members (only 5,000 “vested”)
- EORP (Elected officials, judges and court commissioners)
  - 2,076 members, system closed to new members in 2013
  - Subject of *Fields* and *Hall* lawsuits
  - Lowest funding level of all plans

Financial Health

Funding % as of	**PSPRS**	**EORP**	**CORP**
FY2016 50. 3 %	41%	59.2%	
Asset losses	(0.6%)	(0.5%)	(0.7%)
Payroll Growth	0.2%	0.9%	1.6%
PBI Gain/(Loss)	0.7%	1.6%	0.8%
Benefit Changes	(2.5)%	0.0%	0.1%
Assump.changes		(1.9)%	(1.2)%
(2.4)%			
Other 1.1%	(2.0)%	0.7%	
FY2017 47.3%			

Under pressure

Financial health at a glance



What happened?

Perfect storm

- Investment losses
  - 2001-2002 "Dot.com" loss of $1 billion
    - Funding level decline to 100.9 percent from 126.9 percent
  - 2008-2009 "Great Recession" crunch
    - FY 2010 funding level drops to 65.8 percent
- Permanent Benefit Increase
  - Based on year-to-year investment returns
  - No funding level requirement
  - Period of high returns

What happened (cont.)?

PBI under the microscope

Fiscal Year	Investment Return	Monthly PBI (in $)	Aggregate Funding Level
2000	12.31%	87.37	124.70%
2001	-16.86%	93.24	129.90%
2002	-15.07%	98.17	113.00%
2003	6.67%	102.53	100.90%
2004	14.97%	111.90	92.40%
2005	9.11%	116.82	82.10%
2006	8.30%	121.76	77.00%
2007	17.05%	127.06	66.40%
2008	-7.27%	134.34	66.50%
2009	-17.73%	138.66	68.20%
2010	13.47%	146.74	65.80%
2011	17.37%	152.84	61.90%
2012	-0.79%	159.13	58.60%
2013	10.64%	121.19	57.10%
2014	13.28%	65.20	50.40%
2015	3.68%	0.00	49%
2016	0.60%	0.00	47.3%

Litigation

2011 pension reforms (SB1609)

- Second employee tier with more modest benefits
- *Fields* lawsuit, decided Feb. 2014
  - Strikes PBI conditions
  - Impacts EORP and PSPRS
  - Expected cost exceeds $300 million
- *Hall* lawsuit, decided Nov. 1016
  - Strikes increased contribution limits, PBI conditions
  - Likely impact on EORP and PSPRS
  - Possible immediate cost of $200 million

Fortunate timing

2016 reforms in S1428 and Prop 124

- Creation of third employee tier starting July 1, 2017
- Voter passed replacement of retiree PBI with COLA
- Mitigates ongoing expenses/losses of *Hall/Fields* lawsuits
  - Interrupts post-Hall lawsuit effects w/ 2018 COLA intro
  - Long-term savings expected to reach $475 million
  - Savings instead of losses exceeding $1 billion

Question 1

Q. Why are they projecting a 7.5% return on investment when historically they've only realized a 6.5% to 6.6% return?

A. Each .25% drop in the estimate leads to a spike in annual contribution rates. One of the reasons the rates increased so much for next fiscal year is that they dropped their projections .35%.

Question 2

Q. Why do they continue to project a cross the board 4% increase in salary growth when the number seems unattainable in our current environment?

A. Payroll growth includes salaries, overtime, merit increases, promotions, and membership growth. The assumption is reviewed every 5 years.

Question 3

Q. What does this mean for the 10-year projections they provided?

A. While this years actuarial report projects a 1% increase for each of the next 10 years, we feel that at least for the next couple of years 3%-4% may be more accurate.

Question 4

Q. Was the Hall case part of the spike for next fiscal year?

A. According to PSPRS, the spike is $2/3^{rd}$ the result of Prop124 reform, and $1/3^{rd}$ due reducing the projected earnings rate from 7.85% to 7.5%

Question 5

Q What are the projected impacts of the Hall Case?

A. Should be minimal. SB1609 increased the rates for the employees with the caveat that it could not impact the rate for the employer. This means that the actuarial estimates have never included the additional 4% employee contribution.

Question 6

Q. When will the Hall and Parker cases be settled and how will it be paid out?

A. Could be anywhere for 6-12 months. PSPRS will figured amounts owed. The agencies will be responsible for paying the employees, and then will be granted a PSPRS holiday until the agency is net neutral

Question 7

Q. We thought PROP 124 was supposed to lower costs long term. Why the big impact and where did the legacy cost come from for Tier 3?

A. PROP 124 will lower costs over time, however the COLA is now figured as part of the actuarial and the legacy costs exists because Tier 1 and 2 retirees must be funded

Tiers

- Tier 1 and 2 in the simplest terms is separated by a wall
- No additional employees will be added to these two tiers, but they must still be funded
- New in Tier 2 is a 3% split, with a catch up provision costing employers 4% over a period of years. The intent is to balance non-SS employers with SS employers

Tier 1 and 2

- All new tier, not tied to Tiers 1 and 2
- Employees have the option of either DB plan or DC plan

Tier 3

Tier 3

- DB plan is 7.13% employee/employer + a 3% split for SS
- The 7.13% has no cap as far as future increases, but increases will be split 50/50 between employer and employee
- No DROP program
- 10 year vest

Tier 3

- DC option is a 9% employee/employer split + 1.17% long term disability split + a 3% split of SS
- The 9% will not increase
- 10 year vest period
- What you have in the account at retirement is what you have – no guaranteed benefit amount

Municipal Agencies/Districts

- Municipal agencies and Fire Districts are two different types of political entities within AZ
- Each has different funding mechanisms which means their approach to fiscal issues is different
- Most municipal governments are far older than Fire Districts meaning their pension liabilities are, in many cases, far greater
- Each must look for solutions to ease the PSPRS burden within the options they have available under current statute.

Conclusion

- We have little control over costs associated with PSPRS
- There is no light switch solution
- A State wide tax to cover costs would alleviate pressure, but is unlikely at this point
- Costs will continue to increase, but should be more manageable after this next fiscal year
- Will take years to fix funding levels and bring costs down
- We as an organization will be the ones to feel the ire of the public as we adjust to pay the expense