

TMRS Update April 2008

Opportunities and Challenges Facing The City of Arlington and RETIREES

Things are changing at the Texas Municipal Retirement System. Cities and TMRS are working closely to develop strategies for future funding of the system. Eric Henry, the system's new executive director, is part of TMRS' new approach.

TMRS Facts

- **Founded in 1948**
- **Arlington's Membership Began in 1961**
- **TMRS has more than 800 Member Cities and More than 130,000 Participants**
- **TMRS Is Responsible for More than \$14 Billion in Assets**

Henry and the board of TMRS are developing a new strategic plan for the system that will involve making changes in the pension contributions and the methods for determining long-term liabilities. Cities and TMRS are working to continue to provide a competitive retirement benefit as well as funding methods that minimize the increasing financial impact on member cities. (See Henry's biography on page 4)

Providing A Competitive Retirement in Challenging Times

As you know, TMRS has been recognized for its financial stability for many years. However, changes in the economy, are causing TMRS to reconsider their stable, yet conservative investment approach. With its primary investment being in high-quality corporate, government and agency bonds, TMRS has recently seen a decrease in interest income that previously assisted in funding the system.

Arlington is facing its own challenges. The City is reaching build out so the workforce is not increasing significantly, limiting the number of active employees contributing to the system. In 1997, the City had 2,229 active employees contributing to the system. In 2006, 2,271 were contributing. During that same period, the number of retirees, who are no longer contributing to the system, increased by 151% from 339 to 852. Payroll increases, which obviously augment funding provided for retiree benefits, have been limited in recent years. TMRS has assumed a 5% increase to payroll and particularly in the early 2000s, employees simply did not receive that level of pay increase.

The economy and our changing demographics are requiring changes in our future planning for TMRS.

Arlington's Challenges

- Community Reaching Build Out
- Stable Workforce Size
- Limited Growth in Payroll
- Increasing Number of Retirees



Your Benefit

Arlington has adopted the greatest benefit options available through TMRS (see plan provisions at right). These include the highest rate of employee contributions and a 2 to 1 city matching ratio with the full menu of options available to cities.

Discretionary Benefits

Updated Service Credit

Improves the retirement benefits for active employees by using the average monthly salary of a member over the final three years of the employment and calculates the member's retirement credit as if that member had always earned that salary. This mitigates the affects of inflation on employees retirement credits. (Example: An employee starts working for the City in 1980 and earns \$20,000 a year. Throughout the employees career, he or she has received raises. The employee retires in 2000 and for the last three years of their employment they make \$40,000 a year. Their retirement credit will be calculated as though they had made \$40,000 annually for their entire career.

Annual Annuity Increase

Allows retirees to keep up with Cost of Living increases. Annually, the City can elect to provide cost of living increases for retirees. The City's current election is to provide retirees with adjustments equal to 70% of the annual increase to the Consumer Price Index. If the City were unable to provide this or a like benefit, then a retiree who receives a monthly check of \$1,000 at the time of retirement, would have a monthly check would be worth about \$500 in 20 to 30 years, because of the inability to adjust for inflation.

These benefits are discretionary because they can be approved or denied by the City Council annually.

Arlington's Plan Provisions Are:

- Employee Contribute – 7%
- City Matches Contribution – 2 to 1 (14%)
- Repeating Updated Service Credit
- Repeating Annual Annuity Increases - Based on 70% of CPI
- Military Services Credit
- Vesting at 5 Years
- 20 and Out
- Supplemental Death Benefit

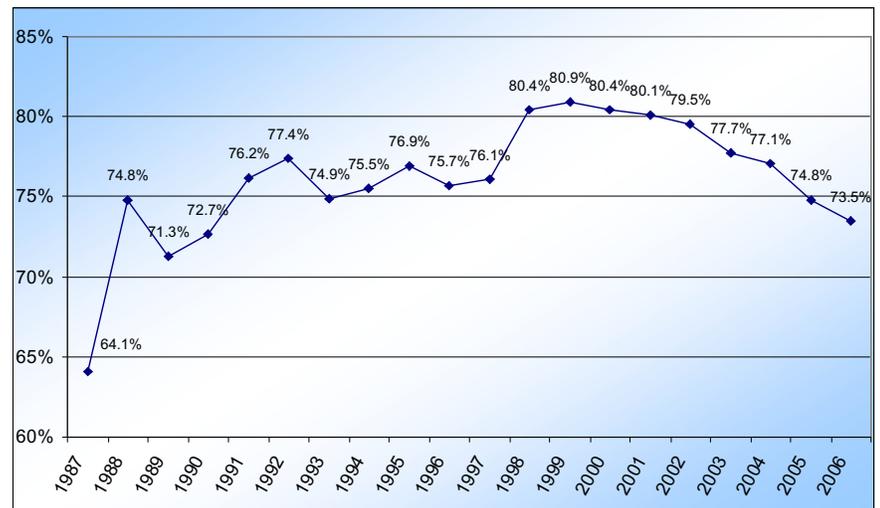
Defined Contribution or Defined Benefits

TMRS is primarily a defined contribution plan. This means that the money that the employee and the City contribute to the system, as well as interest earned on that money, completely fund an employee's retirement. Employees are not promised a set benefit. Their benefit is calculated on what has been contributed for them at the time of retirement.

However, there are two components to TMRS that have characteristics of a defined benefit plan - Updated Service Credit and Annual Annuity Increases for retirees. (COLAS - Cost of Living Adjustments. See a description of these benefits at left.)

These benefits are provided to assist the employee and retiree with handling inflation. However, the City and the employee during the employee's work life have not contributed an amount adequate to fund these benefits. Consequently, when the economy and interest payments are lagging and the City's demographics are changing, as mentioned in Arlington's Challenges, a funding gap is created.

Arlington's History of Retirement System Funding

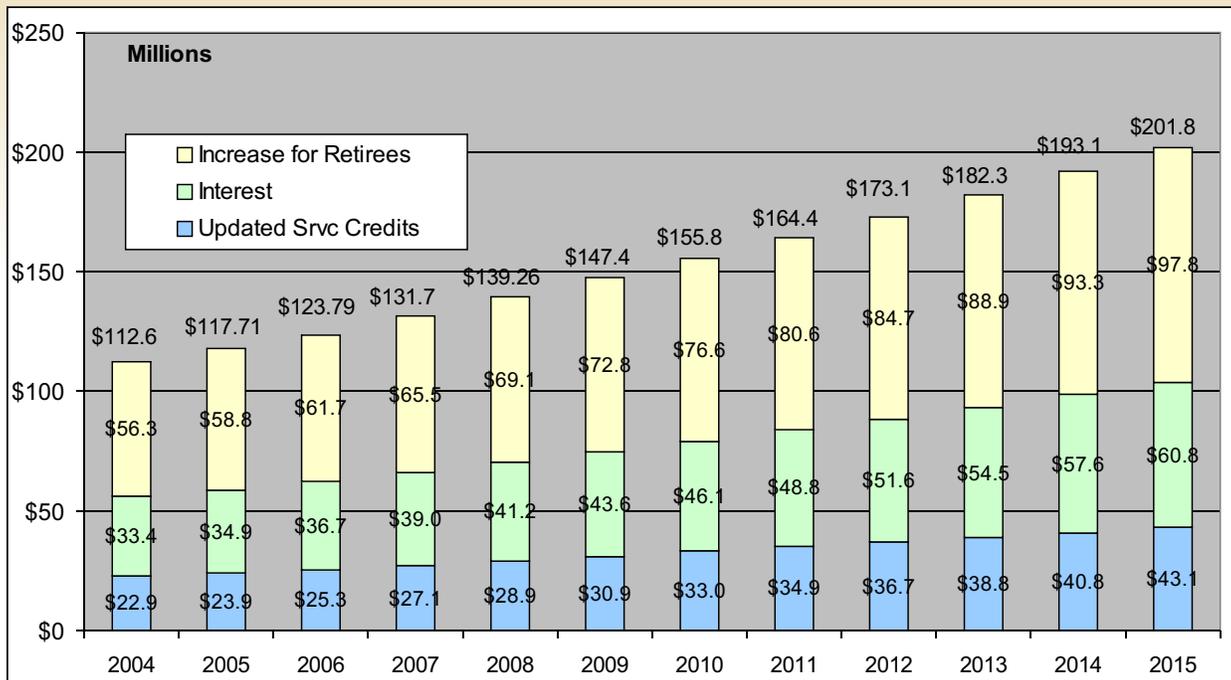


As you see, the City's funded coverage of its long-term liability has been decreasing in recent years. This has primarily been caused by a lack of funding for Updated Service Credits and the Annual Annuity Increases. A better, healthier funding would be 80-100%.

Our Funding Gap

A significant gap in funding has occurred in recent years between what the City and the employee are paying and what will be needed over the next several decades to adequately fund employee retirements. This has resulted in a decrease in the amount that the City's retirement system is funded. As mentioned earlier, ideally, the City would have invested enough to cover 80 - 100% of its long-term needs.

Cost Drivers of Arlington's Gap (Source: First Southwest Co.)



As seen in the chart above, the primary drivers of Arlington's funding gap are the annual increases given to retirees, the Updated Service Credit benefit, and the interest income the City is not making because the plan is not fully funded.

For example, in 2004, the City needed an additional \$112.6 million to fully fund its TMRS liabilities. About \$56 million of that gap was created by annual increases to retirees, and about \$23 million was created by

Updated Service Credit. If the City been able to fully fund these two benefits, the interest we could have accrued would have been about \$33 million and would have helped us close the gap.

Because the gap is caused primarily by Updated Service Credits and the annual increase for retirees, both active employees and retirees may be affected by the ultimate plan the City develops.

City of Arlington TMRS Employee Taskforce

An employee taskforce has been appointed to work with city management on a long-term plan for TMRS, and this plan will be presented to the City Council as part of the FY 2009 Budget Process.

Employees were selected from across the City and across job families. They include:

- Pam Williams (Development Services and Planning)
- Paul Kelso (Parks and Recreation)
- Gary Gilliland (Water Utilities)
- David Crow (Fire)
- Randle Meadows (Police)
- David Fox (Public Works and Transportation)
- Karen Taylor (Workforce Services)
- Karen Vanwinkle (Airport)
- Pamela Hutson (City Attorney's Office)

Eric Henry **TMRS Executive Director**

Eric Henry was appointed Executive Director of the Texas Municipal Retirement System on April 27, 2007 by the Board of Trustees, and began his position there effective June 11, 2007.

Before coming to TMRS, Mr. Henry was the Executive Director of Pennsylvania State Employees' Retirement System (SERS) since 2004 and also served at SERS as Director of Internal Audit and Assistant Executive Director from 1994 to 2000.

Before his appointment to Executive Director at SERS, he was Executive Director and Chief Investment Officer for the New Hampshire Retirement System from 2000 to 2004.

Mr. Henry holds a Bachelor of Science degree in Accounting from Penn State University and a Master of Business Administration degree from Bucknell University.

He is also a Certified Information Systems Auditor and a Certified Public Accountant, and has received the Certificate of Achievement in Public Plan Policy from the International Foundation of Employee Benefit Plans (IFEBP).

In Summary

We will be working with TMRS over the next several months to outline a strategy and plan for providing a competitive retirement benefit that both the City and the employee can afford.

Next Steps for TMRS and the City of Arlington

- Communicate to Mayor and City Council
- Communicate to the Workforce and Retirees
- Continue Working With TMRS As a Member City on Changes That Will Improve Our Position
- Report to Mayor, City Council, and City Workforce on Progress Throughout the Year
- An Employee Taskforce has been appointed and will work with City Management on a long-term plan for TMRS that will be presented to the City Council as part of the FY 09 Budget process.

TMRS CONTACTS

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