City of Houston

Presentation to the State Pension Review Board of Texas

Sustainable City of Houston Pensions

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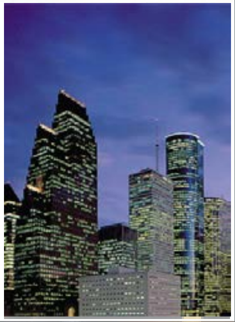
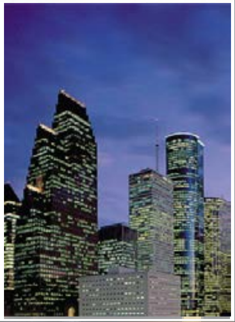


Overview

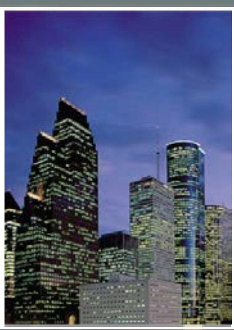
- Background
  - Mayor’s commitment: Fair, affordable and sustainable pensions
- Houston’s plan
  - Be clear about what the City owes
  - Reduce liability
  - Manage costs going forward
- Cost management: The corridor
- Next steps



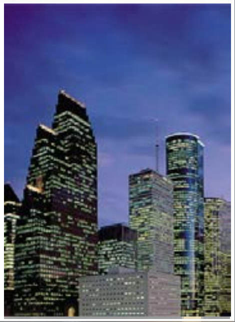
Background

- Pension reform a priority for Mayor Turner
- Three objectives for now and in the future
  - Reduce costs
  - Reduce unfunded liability
  - Achieve a solution that removes pension issues from the table
- Employees, retirees and taxpayers deserve a pension system that is fair, affordable and sustainable
- Shared sacrifice is required to meet the objectives
- Nearly a year of working closely with pension system representatives

Houston’s Plan: What is owed?



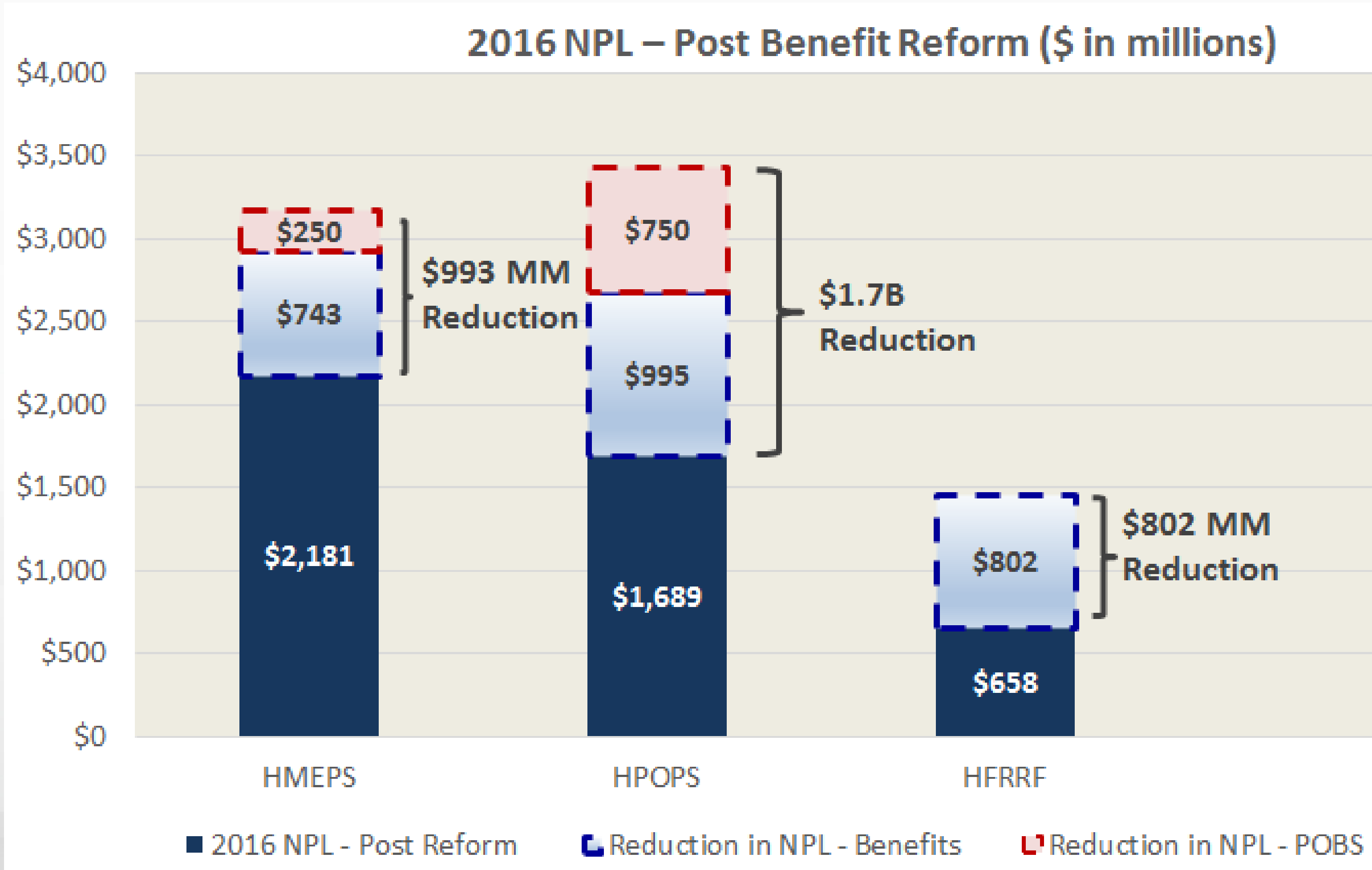
- First step: Get a clearer look at what we owe
- Requires more accurate calculation of City’s net pension liability
  - Reduce anticipated rate of return (i.e., discount rate) for all three systems to 7 percent
  - Recognize all investment and other actuarial gains and losses as of June 30, 2016
- Impact: Increase City’s pension liability from \$5.6 billion to \$8.1 billion

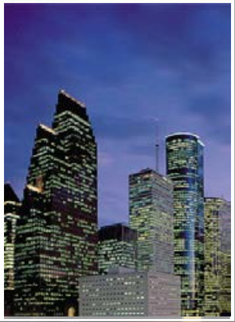

Houston's Plan: Reduce liability

- Second step: Reduce the City's pension liability
  - Benefit adjustments in all three systems to reduce future costs: liability reduction of $2.54 billion
  - City addresses past underfunding with issuance of $1 billion in POBs
    - HMEPS ($250 million) and HPOPS ($750 million)
  - City required to make full annual contributions to each system: no more long-term underfunding
- Impact: Total immediate reduction in net pension liability of $3.54 billion

Houston's Plan: Reduce liability



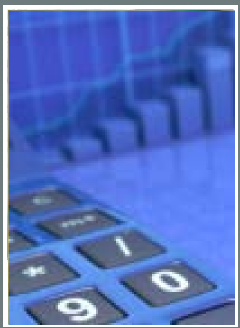
Sources: City of Houston January 2017 actuarial reports for HMEPS and HPOPS; COH-HFRRF term sheet.


Houston's Plan: Manage costs

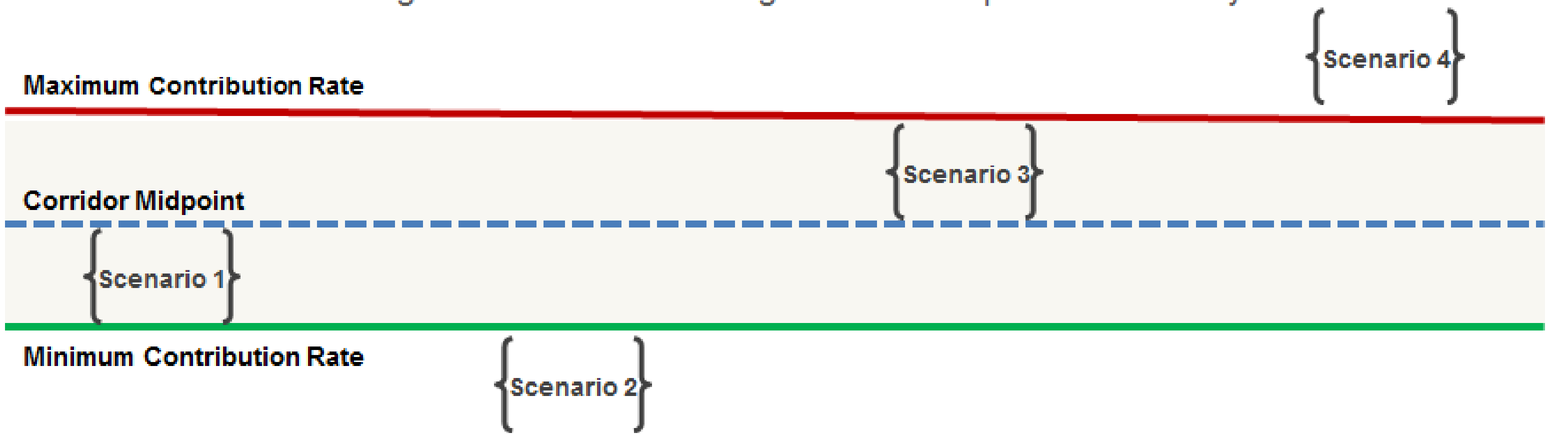
- Third step: Better management of pension costs and liability in the future
  - Closed 30-year amortization sets clear schedule and hard date for payoff: no more "kicking the can"
  - Corridor sets City contribution boundaries that trigger pension system changes if breached

Houston's Plan: The corridor



Overview of Risk Sharing

The Corridor is a cost management mechanism designed to ensure plan sustainability



Declining Pension Costs		Rising Pension Costs	
Scenario 1: Inside Corridor – between Midpoint and Minimum	**Scenario 2: Outside Corridor – Below Minimum**	**Scenario 3: Inside Corridor – between Midpoint and Maximum**	**Scenario 4: Outside Corridor – above Maximum**
•City Contribution Rate is in between Minimum and Midpoint •If system <90% funded, City contribution remains at midpoint •Otherwise, City contributes at rate needed to fully fund the system	•City Contribution Rate is below Minimum •Bring City Contribution Rate back to Minimum by making system adjustments in order proscribed by law (e.g., recognize market losses if doing so increases contribution rate)	•City Contribution Rate is in between the Midpoint and the Maximum •City contributes at higher rate needed to fully fund the system	•City Contribution Rate is above the Maximum •Move City contribution rate back within corridor with system adjustments (e.g., use prior overfunding) •May also require benefit changes to bring contribution rate to Midpoint over a three year period

Corridor Midpoint = proposed benefits package estimated cost

Next steps

- Rep. Flynn has submitted agreed-upon legislative language and term sheets to Texas Legislative Council
- Coordinating with Senate sponsor Sen. Huffman
- Bill is to be presented as committee substitute for HB 43