

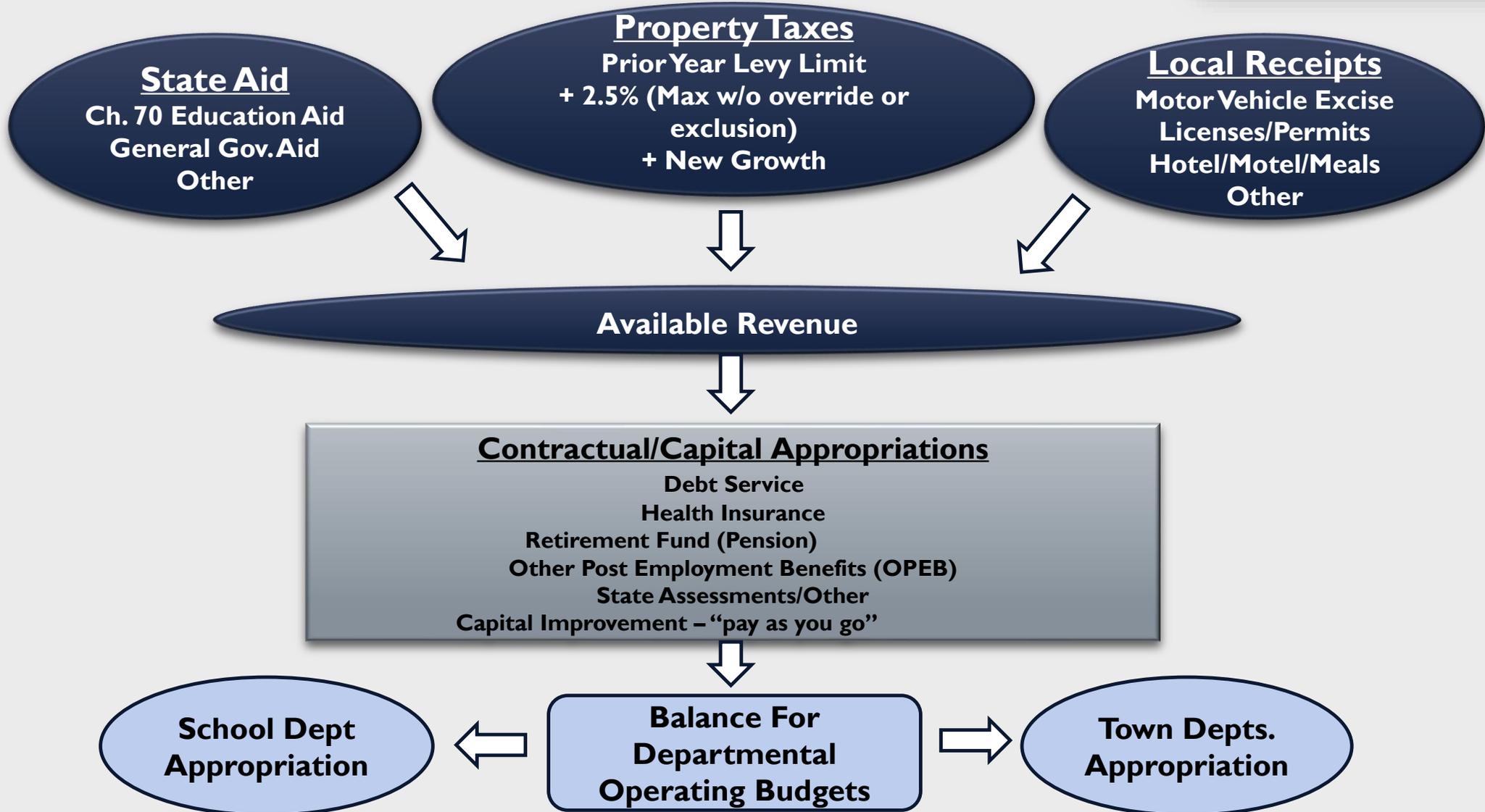
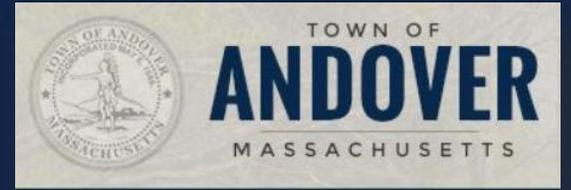


TOWN OF ANDOVER

Andrew P. Flanagan, Town Manager
November 4, 2019

TOWN OF ANDOVER BUDGET MODEL

(EXCLUDING WATER/SEWER/OFFSET LOCAL RECEIPTS)



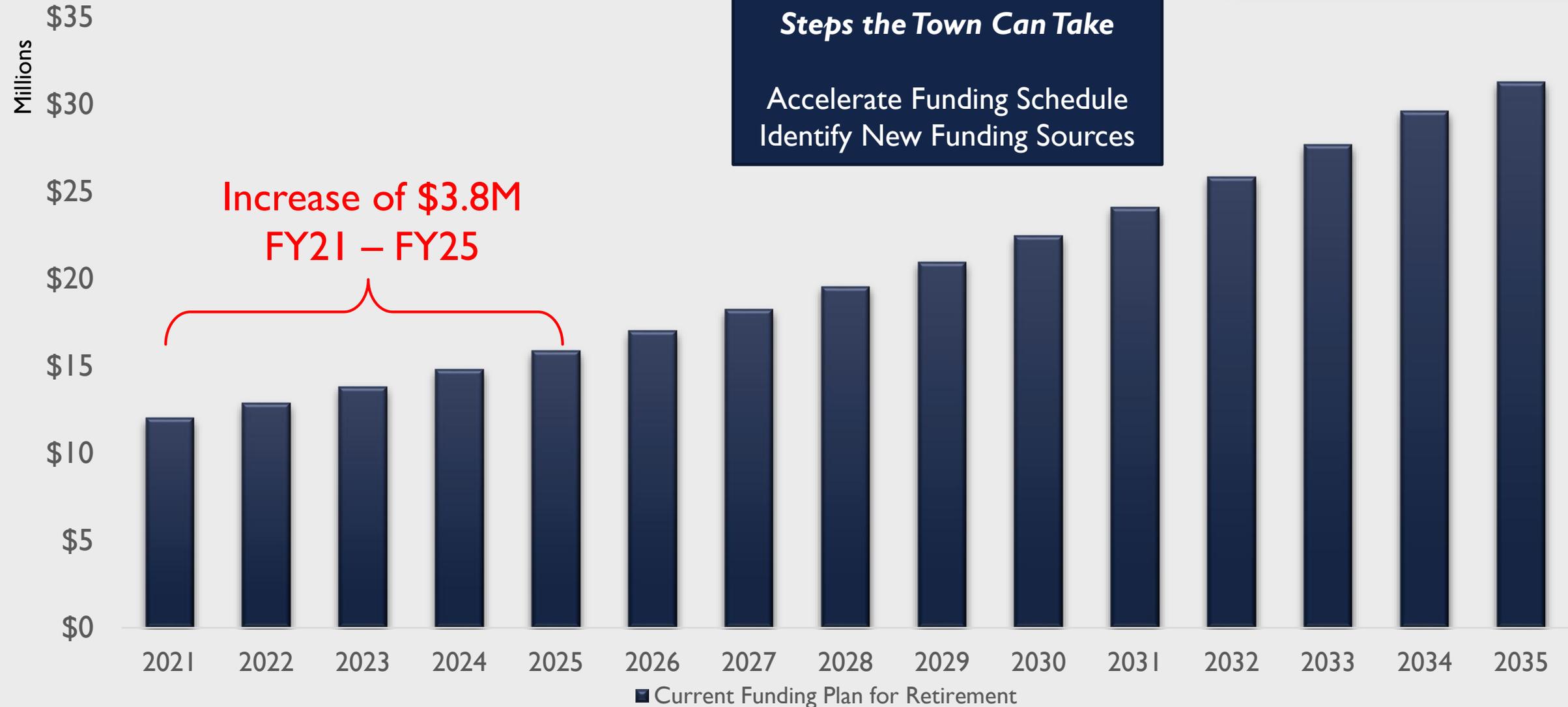
RETIREMENT FUNDING SCHEDULE



Steps the Town Can Take

- Accelerate Funding Schedule
- Identify New Funding Sources

Increase of \$3.8M
FY21 – FY25



Pension Update

November 4, 2019

Hayley Green

Thomas Hartwell

Agenda

- Membership Eligibility
- Buybacks
- Why reforms are necessary
- Discount rate
- Investment performance

Membership Eligibility

- Currently, any permanent employee working 20 hours or more per week is eligible to join the system. Additionally, individuals or elected officials must earn at least \$5,000 per year in regular compensation and elected officials don't need to satisfy the 20 hours per week minimum.
- There has been discussion on changing the minimum to 35 hours per week or keeping 20 hours and prorating creditable service.
- We are waiting for the actuary to provide the financial impact.
- We plan to hold a separate meeting with all stakeholders to discuss their concerns on the effect of changing eligibility.

Examples of plans requiring greater than 20 hours eligibility

- **Reading** – Anyone whose total service for their primary position equals or exceeds 1,690 scheduled hours per year. The primary position is defined as the position with the highest number of hours. It may not be combined with any other position.
- **Wakefield** – All permanent employees who are employed on a regular work week for not less than 30 hours a week.
- **Methuen** – The individual works a minimum of 30 hours a week, for a minimum of 40 weeks a year.

OBRA and Massachusetts Deferred Compensation

An alternative to Social Security is permitted by the federal Omnibus Budget Reconciliation Act of 1990 (OBRA).

- Part time, seasonal or temporary employees not eligible to participate in the employer's retirement program are required to participate in a Massachusetts deferred compensation plan. Andover uses a 457 plan with ICMA-RC.
- Employees contribute at least 7.5% of their gross compensation to the plan.
- Contribution is deducted on a pretax basis.
- Additional contributions above the mandatory contribution of 7.5% are allowed.

Proposed Regulation for Buybacks

- Currently, anyone with prior ineligible service who becomes an eligible member of the system can buy back that prior time based on 20 hours per week or 86.67 hours per month being full credit.
- The proposed regulation will not allow future employees to buy back prior part time service.
- Some MGLs require us to allow prior service buybacks (i.e. military, other municipalities) but we have the control to determine how to calculate it. Proposed to prorate the time based on 35 hours per week or 151.67 hours per month.
- We are waiting for the actuary to provide the financial impact. The public hearing in August was suspended and will reconvene at a future meeting.

Why reforms are necessary

- The retirement plan has one of the lowest funding ratios (48%) in the State (94th out of 104 plans) and one of the lowest in the country (public plans nationally average 72%).
- Andover (our Sponsor) incurred losses of **(\$12.3 million)** for FY 2018 and **(\$13.5 million)** for FY 2017. Losses are principally due to pension and OPEB expense. Losses are expected to continue going forward.
- Andover's negative net position (liabilities exceeding assets) was **(\$65.4 million)** at 6/30/18.
- Actuary's valuation report as of 12/31/18 prepared shows pension unfunded liability (using 6.25%) increased from \$163 million at 12/31/17 to \$180.9 million at 12/31/18.

Other Post employment Benefits (OPEB)

- Changing the eligibility for participation in the retirement plan also affects participation in OPEB. In order to qualify for OPEB, an employee needs to be in the retirement plan.
- Questions were posed to our OPEB actuary to help assist in the analysis. The actuary, to date, has been unresponsive. The latest (FY 2018) actuarial valuation report show normal cost of \$3.8 million with 1,357 active employees. This averages \$2,800 annually in cost to the town per employee. Actual OPEB expense for 6/30/18 was \$13,446,602 which includes interest, differences between expected and actual experience, and changes in assumptions.

Pros & Cons of Changing Eligibility

- Pros

- Would reduce cost per future employee to the Town by \$5,000 - \$10,000 annually, which should help in addressing the town's future costs. The actuaries will need to determine the actual savings.
- Would slow down the future growth of pension and OPEB unfunded liabilities.
- Would eliminate future market risk to the town for these employees if long term rate of return/discount rate projections and other assumptions are not achieved.

- Cons

- May affect the town's ability to hire and retain employees

How Andover stacks up with other plans

	2004 funding ratio	2018/2017* funding ratio	% increase, (decrease)	2018/2017* discount rate
Leominster	67%	100%	33%	5.50%
Dedham	75%	94.7%	19.7%	7.50%
Lexington	84.7%	87.2%	2.5%	7.50%
Concord	82.4%	86.5%	4.1%	7%
Winchester	78.9%	84%	5.1%	7%
Wellesley	103.5	81.3%	(22.2%)	6.625%
Norwood	80.5%	80.6%	0.1%	7.75%
Reading	68.9%	73.8%*	4.9%	7.625%*
Needham	73.1%	68.2%	(4.9%)	7.25%
Newton	67.6%	51.7%	(15.9%)	7.25%
Arlington	61.5%	51.5%	(10%)	7%
Andover	78.1%	48.6%	(29.5%)	7%

Discount rate

- The town currently uses a discount rate of 6.25% at 6/30/19 in valuing pension liabilities.
- The retirement board used a 7% discount rate in valuing pension liabilities as of 1/1/18.
- The retirement board will set a new discount rate as of 1/1/20.

Discount rate/long term rate of return

Period	Retirement Board Discount Rate (Geometric)	Actual Investment Return (Geometric)
5 Years (2014- 2018)	7.40%	5.58%
10Years (2009 – 2018)	7.65%	8.39%
20Years (1999 -2018)	8.02%	4.39%

\$\$\$ impact if Retirement Board uses 6.25%

	7%	6.25%	% Change	\$ Change
Employer Contribution				
1. Normal Cost	2.7	3.9	44.4%	1.2
2. Amortization Payment for UAL	8.5	7.5	(11.8%)	(1.0)
3. Employer Contribution (1+ 2) for 2020	11.2	11.4	1.8%	0.2
4. Projected Employer Payments 2020 – 2035	317.6	382.9	20.6%	65.3
5. Accrued Liability	282.3	306.7	8.6%	24.4
6. Market Value of Assets	143.8	143.8	0%	0
7. Unfunded Accrued Liability (UAL)	138.5	162.9	17.6%	24.4
8. Funded Ratio (6/5)	50.9%	46.9%		

Investment performance

- As of 9/30/19, total return since 1/1/18 is approx. 4.65% (net of fees).
- If the plan had earned 7% annualized as projected by the retirement board through 9/30/19, investment return would be approx. \$5 million greater than what was actually earned.
- The three month return that would be needed in order to link up with the 21 month period to generate an annualized rate of 7% over 24 months would be in excess of 10%.