



# Public Safety Pension Funding

April 9, 2019

Village Board of Trustee Meeting

# Finance Committee Review

- For the past two years, the Finance Committee has been reviewing strategies to address the Village's public safety pension challenges with the following goals in mind:
  - Eliminate the unsustainable “ramp up” of contributions by leveling out/stabilizing future contributions
  - Provide a long-term solution that will ensure increasing pension contributions do not prevent the Village from funding other critical needs such as roads
  - Preserve the Village's Aaa bond rating by addressing what Moody's has noted as a credit challenge – “high pension burden”

# Finance Committee Recommendation

- The Finance Committee is recommending that the Village transition to an open 15-year rolling amortization for public safety pensions
- This is a long-term strategy to address the Village's unfunded pension liability in a pro-active and manageable way
- This method will provide a more predictable framework to view pension needs as we think long term for the Village
- The change will require increased contributions in the short term, but over time, will significantly reduce the Village's funding requirements

# The Village's Pension Challenges

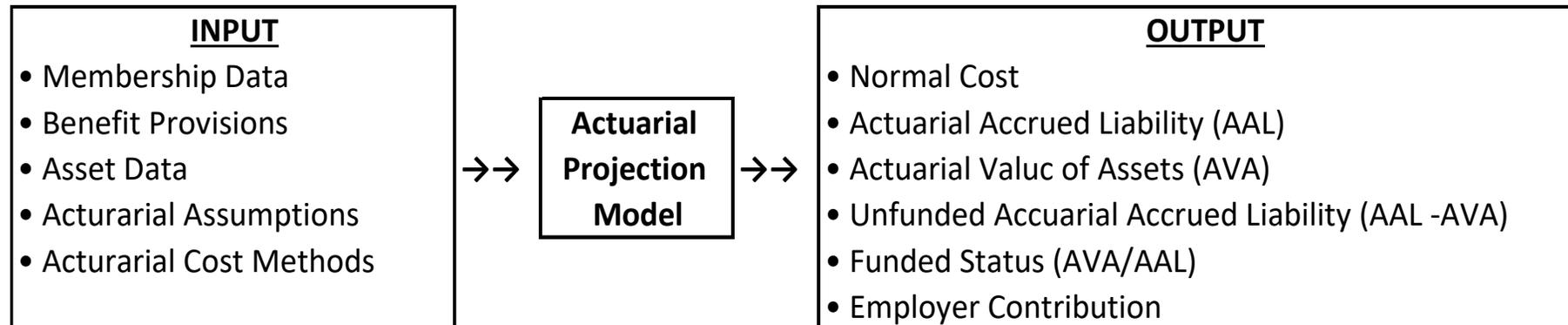
## What does the Village Control?

- Pension Benefits are established by the State: (Liability)
  - Years of service to obtain a benefit
  - Amount of benefit
  - Survivor benefits
- Pensions are funded by: (Assets)
  - Employee contributions – established by the State
    - Police - 9.91% & Fire - 9.455% of pay
  - Investment returns – Types of investments established by the State, managed by Pension Funds, varies based on market returns
  - Village contributions – “fund the balance”: minimum required contribution dependent on actuarial calculation

# Actuarial Valuation

## Employer Contribution

- The actuarial valuation is performed on an annual basis
- Purpose of valuation:
  - To determine the amount needed to fund benefits over time
  - To measure the plans funding status



- $\text{Employer Contribution} = \text{Actuarially determined contribution} - \text{Employee contribution} - \text{Investment Returns}$

# The Village's Pension Challenges

## Growth in Village Contributions

- Despite responsibly funding public safety pensions, costs have continued to escalate

	1998	2019	2024 projected
<b>Village Contribution</b>	\$596,800	\$5,096,000 754% increase	\$6,037,000
<b>Pensions as a % of Tax Levy</b>	8%	27%	
<b>Pensions as a % of General Fund Expense</b>	3%	14%	
<b>Total Pension Liabilities</b>	\$-2.7 million (over funded)	\$56.5 million under funded	\$65 million under funded
<b>Funded Status</b>	Police: 105.67% Fire: 106.90%	Police: 64.60% Fire: 60.80%	Police: 62.6% Fire: 60.60%

# The Village's Pension Challenges

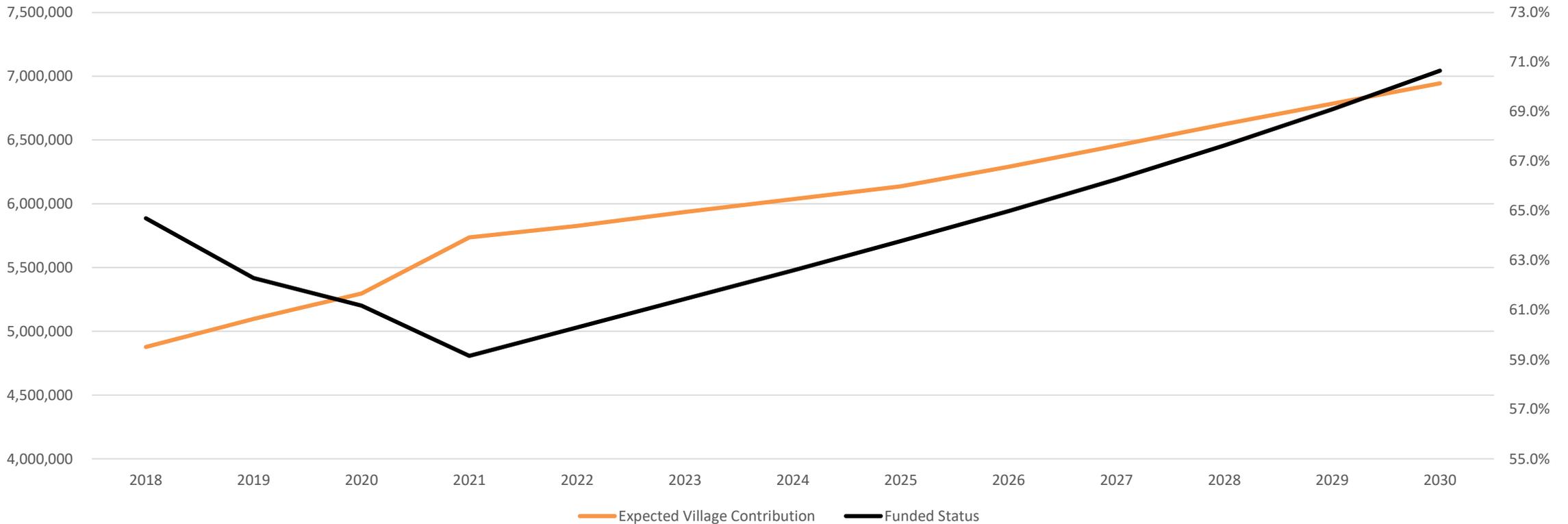
## Current Funding Policy

- State law, through a political process, has set an arbitrary date for public safety pensions to be funded
  - 90% by 2040
  - Village policy is to be 100% funded by 2040
- This type of “closed” funding system is not prudent and will lead to unmanageable increases in contributions leading up to 2040
- While the State has previously extended the deadlines for funding, such deferrals only serve to grow total liabilities and subsequently lead to greater increases in future pension costs

# The Village's Pension Challenges

## Current Funding Policy

Village Contribution & Funding Level Trend  
Current Policy



Contributions are projected to exceed \$9 million by 2040, an 80% increase

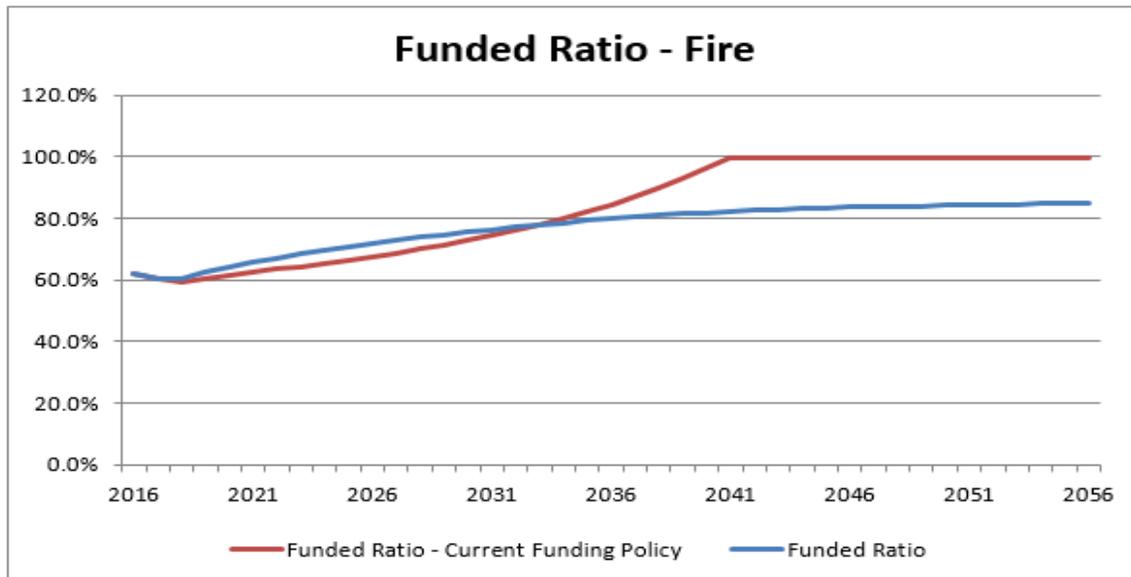
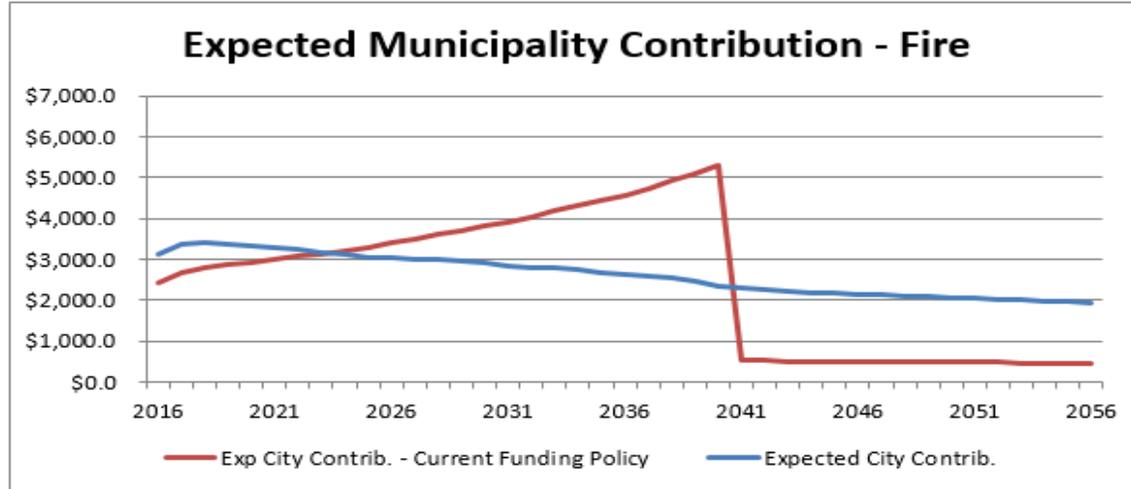
# The Village's Pension Challenges

## Strategies Considered by the Finance Committee

- The Finance Committee reviewed a number of potential ways to address the Village's pension challenges:
  - Make no changes and hope the State of Illinois provides pension relief
  - Change the assumed rate of return (currently at 7.25%)
  - Implement an open 20-year rolling amortization in FY 2020
  - Transition to an open 20-year rolling amortization between FY 2020 – 2023
  - Implement an open 15-year rolling amortization in FY 2020
  - Transition to an open 15-year rolling amortization between FY 2020 - 2023
- The Finance Committee determined that the transition to an open 15-year rolling amortization was the preferred option to truly address the Village's long-term challenges, while doing so in a manner that limited the immediate impact to Wilmette taxpayers

# Revised Funding Policy

## Open Amortization Model



### Key Points

- An open schedule (blue line) means the amortization period would be continuous and reset every year to a rolling 15-year period
- While the fund will never be 100% funded, it will eventually reach and maintain 80 – 90% funding (this is considered a healthy level)
- Contributions are projected to increase in the short term to a high of \$6.5 million in 2023, after which they should steadily decline to less than \$4 million by 2040
- Addressing the unfunded liability is seen as a credit positive by Moody's

# Long term Impact of Open Amortization

<b>Total Village Contributions from now to Closed 2040</b>	
	Public Safety Contributions (\$)
Current Closed Funding Policy	147,000,000
Proposed Open Funding Policy	109,000,000
<b>Difference in Village Contributions</b>	<b>38,000,000</b>

<b>Total Village Contributions from now to Closed 2050</b>	
	Public Safety Contributions (\$)
Closed Funding System	224,000,000
Proposed Open Funding Policy	146,000,000
<b>Difference in Village Contributions</b>	<b>78,000,000</b>

## Key Points

- The open system is less costly to the Village over time
- An open system is preferred by bond rating agencies because it makes future pension contributions more manageable while paying down the unfunded liability
- The longer the Village waits to change amortization schedules, the more costly the change becomes
- Even if the Illinois General Assembly extends the deadline to reach 90% funding to 2050 as is currently contemplated, the open system is still the best option

# Moody's Credit Analysis of the Village

## October 2018

- Credit Strengths
  - Very affluent community
  - Home rule status
  - Healthy operating reserves relative to budget
- Credit Challenges
  - High pension burden
  - Exposure to economically sensitive sales and income tax
- Factors that could lead to a downgrade
  - Further growth in pension or debt burden
  - Failure to continue strengthening pension contributions as anticipated

# Near term Impact of Open Amortization

- Three year transition to a 15 year open amortization policy
- The open system is projected to require an additional \$1.4 million in pension contributions between 2020 – 2023 as compared to the current policy

<b>Contribution Method</b>	<b>2019 (\$)</b>	<b>2020 (\$)</b>	<b>2021 (\$)</b>	<b>2022 (\$)</b>	<b>2023 (\$)</b>
Current/Baseline	5,096,000	5,296,000	5,737,000	5,826,000	5,936,000
Transition to Open 15-Year Amortization from 2020 - 2023	N/A	5,436,000	6,081,000	6,419,000	6,550,000
Property Tax Dollars Required to Implement the Transition to an Open System	N/A	340,000	645,000	338,000	131,000

# Financing the Transition to Open Amortization

- Pension contributions are paid directly through a dedicated portion of the tax levy, which is the most stable revenue source to meet the Village’s obligations
  - Other sources of revenue such as a sales tax, food and beverage tax, ambulance fees, etc. would not bring in sufficient funds to meet the pension needs, nor would they be considered a stable source of revenue
- To limit the immediate impact to taxpayers, it is recommended that an approximate \$1.25 million of General Fund reserves be utilized to offset portions of the tax levy increase

	Total Property Tax Levy Increase				Total Increase in Property Tax Payments to Village from Current Proj.
	2020	2021	2022	2023	
<b>Current Projection</b>	3.78%	3.10%	3.34%	3.61%	
<b>Recommendation</b>	3.85%	4.21%	4.32%	5.64%	+150
<b>Projected Reserve Drawdown</b>	\$200,000	\$500,000	\$500,000	\$50,000	

# Next Steps

- The FY 2020 Budget will be prepared assuming the transition to an open 15-year rolling amortization for the public safety pension funds
  - Given the Village’s positive General Fund reserve position, the recommended pension amortization policy and use of reserves will still allow for additional infrastructure work in FY 2020
- When the Village goes to the bond market for the Neighborhood Storage Improvements, this change will be highlighted to the rating agency and will be a critical component in trying to retain our Aaa rating