As you know, in recent years BERS has been using the Open Group method, as developed by Buck Consulting, to develop annual funding policy contributions. Hooker & Holcombe recommends that BERS not continue with the Buck Open Group calculation method, and instead suggests BERS consider the Direct Rate Smoothing method, which employs a modified open group approach.

The goal is still on appropriately capturing now some of the savings the system will see as staff retire under no longer available and more expansive benefits and new staff are hired with lesser benefits. A key factor of the recommendation is that this is done in a conservative manner that meets accepted actuarial standards and does not put an unjust, significant tax/rate burden, or employee contribution burden, out in the future. Moving from the Buck's Open Group methodology, to the H & H Direct Rate Smoothing with a "Collar," achieves this goal, and does not put us so far outside the norm of other public pension methodologies (as does the Buck's Open Group).

Direct Rate Smoothing

- Is an established actuarial method
- Creates a path toward a pre-defined funding target over a 5-year time horizon. The lower benefits earned by future employees are taken into account, though over a shorter timeframe (modified open group).
    - Valuation would include the normal cost + 20-year amortization of past service liability applied at the fifth year of the step-down period. As defined by actuaries, best practice is a 15-20 year amortization period.
- Provides a higher level of funding cost and stability from year-to-year.
- Better ensures that an unfair burden to pay for costs on future taxpayers or employees

Open Group

- Considers lower benefits earned by future employees over several decades, and amortized over up to 30 years
- Is subject to greater variability of future outcomes due to the 25-30 year time horizon, a timeframe that is longer than actuarially-recommended best practice
- Shifts an inappropriate level of liability for current employee costs to future generations of taxpayers and employees
- Was perhaps implemented more aggressively than we requested of Buck
- Neither H & H or Buck are/were aware of any other public pensions utilizing this method

Direct Rate Smoothing does not define a specific approach, but rather allows for some flexibility in assumptions. Direct Rate Smoothing model would be updated every five years, as each experience study is completed, to ensure assumptions are aligned with plan experience. Direct Rate Smoothing involves a *step down* from the traditional valuation calculated ADEC over up to 5 years.

A modified open group model is proposed whereby for FY 19's contribution we stepdown the open group modified ADEC to 97%, which is in line with our experience with the Buck Open Group method, and a 5-year step down period, which is consistent with the frequency of our experience study. The model would include a collar of +/- $300k, (ADEC can't increase or decrease yearly by more than $300K), which would constrain the year-to-year variability in cost.

With the 97% stepdown, the $300K "collar", ten year smoothing, and other changes currently within and proposed for methods and assumptions, we create a reasonably conservative, and hopefully more stable method to our system that over the next several years should see, subject to an unforeseen significant market downturn similar to 2008/2009, growth in our funding level. BERS can review this approach in conjunction to the soon-to-be completed updated 5 year experience study.

Recommended: 5 Year Step Down from 97% of ADEC

Fiscal Year Ending	Projected City Funding Policy Contribution	Projected Actuarial Value Of Assets*	Projected Funded Ratio
2019	9,878,000	193,774,000	74.7%
2020	9,770,000	204,230,000	75.9%
2021	9,661,000	214,752,000	77.0%
2022	9,553,000	225,260,000	78.0%
2023	9,444,000	235,732,000	79%

*Beginning of fiscal year