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Letter from the Board

- By Vice Chair John Bass

I have been proud to serve not only as Vice Chair of the AFRF Board for 2024, but also as a member of the Working Group tasked with finding a solution to ensure adequate funding and long-term financial stability for our pension. Since the first notification from the Pension Review Board (PRB) alerting the Fund's "at-risk" status for triggering a Funding Soundness Restoration Plan (FSRP), the Board and the Working Group have prioritized consideration of our full membership, including retired, active *and* future members. The Fund prides itself on proactivity and giving voice to members when developing a course of action and remains dedicated to achieving long-term sustainability for the plan.

With the help of the Fund's actuary, Cheiron, through their completion of the 2022 and 2023 Actuarial Valuations and an Experience Study earlier this year, we identified a concerning trend with certain key funding health indicators of the plan. For example, the amortization period has exceeded the 30-year statutory FSRP threshold for two consecutive years and is projected to rapidly increase toward infinite in the coming years, assuming all actuarial assumptions continue to be met. The challenges that the Fund is currently facing are due to structural issues unique to our pension system.

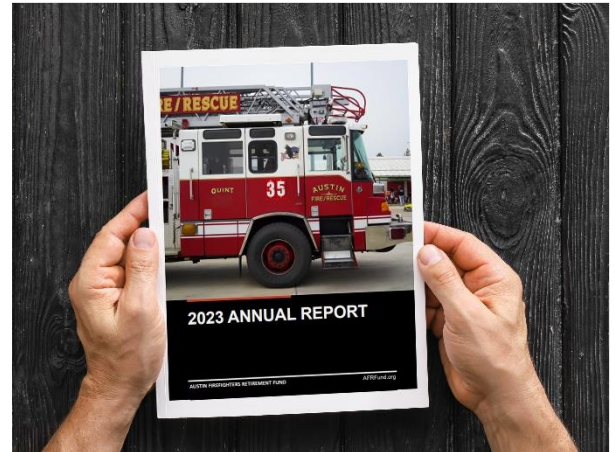
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Letter from the Board, Continued

Two primary drivers include the significant investment losses of 2022 and the aggregate cost of granting Cost of Living Adjustments (COLAs) since 2015, which have been funded entirely through investment gains, gains that are needed to offset future losses so the Fund can meet long term expected returns. While the Fund did have a positive 8.4% investment return for 2023, which helped to recuperate some of the losses from 2022, Cheiron has identified that the current contribution arrangement is no longer sufficient to sustain the benefit structure, and the unfunded liability will continue to grow significantly. Reform has become necessary to avoid triggering the FSRP requirement during the 2024 valuation cycle.

The Working Group has been analyzing this problem from every possible angle and is working to find a long-term solution that addresses these structural issues. It is a difficult task that requires compromise amongst all stakeholders, including the City of Austin, who serves as the sponsor for our plan. At the time of this publication, the Working Group has proposed a pension reform package that offers modest purchasing power protection to retired members and largely preserves promised benefits for actives without shouldering the entire burden on future firefighters. The proposed reforms will need to obtain additional funding from the City, but as of yet, they have not agreed to certain changes. The Board, with the support of its membership, has been vigilant in correcting past challenges to avoid reaching a point of permanent unsustainability. Between the due diligence of this Working Group and the cooperation of our membership, we are confident in our ability to restore plan stability and ensure appropriate funding of our plan into the foreseeable future.

Lastly, an additional area that the Board has been focused on is the responsible management of the Fund's investment program. This year, the Board hired Callan as a third-party consultant to evaluate the governance and performance of the investment program, as required by Texas state law. Callan issued a very healthy report card and stated that our investment program is well-managed. Since last year, the Board has worked hard to reallocate investment gains from public active managers into corresponding passive indexes to capture desired market exposures more efficiently, maintaining expected returns, but with significantly reduced fees. The Board is also in the process of reevaluating its investment approach for the private asset program to consider less costly options, while maintaining exposure to private markets. We are confident that these actions, consistent with finance theory and long-term evidence, will continue to set our investment program on a solid path into the future by reducing fee drag and retaining the Fund's returns where they belong, allowing the Fund to better meet its long-term return objectives.



2023 Annual Report

The AFRF 2023 Annual Report is now available at AFRFund.org. The Annual Report provides important information to help Fund members and stakeholders stay informed about AFRF's finances, including investment performance, funding health, and the operation and management of the Fund. The Annual Report includes the Independent Auditor's Report, the Actuarial Valuation as of December 31, 2023, GASB Statements No. 67 and No. 68, and an overview of the Fund's plan benefits and historical plan provision changes.

At a high-level, the Annual Report indicates that the Fund produced an annual net investment return of 8.4% for 2023, making a positive rebound after the significant economic challenges of 2022, and exceeding the Fund's actuarial return target of 7.3%. The Fund ended 2023 with \$1.16 billion in total market value of assets, a slight increase from 2022. The funded status of AFRF diminished slightly, but remained stable at 85.6%, while the amortization period continued to increase from 35.7 years to 48.6 years, exceeding the 30-year funding guideline established by the Pension Review Board for the second consecutive year. The Fund has not yet triggered a Funding Soundness Restoration Plan (FSRP) requirement but is anticipated to do so following the 2024 Actuarial Valuation. The board remains vigilant and focused on maintaining the long-term funding health of the pension plan. For more information about the FSRP requirement and the board's proactive approach to developing a Voluntary FSRP, please see page 3.

Voluntary Funding Soundness Restoration Plan (FSRP)

The AFRF Board of Trustees' Working Group (WG) has maintained momentum toward the development of a Voluntary FSRP, which aims to proactively address the Fund's increasing amortization period. In January, Executive Director Anumeha Kumar presented at the Actuarial Committee Meeting of the Pension Review Board (PRB), where she emphasized the importance of partnering with both the City of Austin and the Fund's membership to come up with a shared solution that is agreeable for all stakeholders. The PRB was receptive and appreciative of the goal. In June, the WG presented a draft proposal for a pension reform package to the membership for consideration and feedback. In September, the WG followed up with a revised draft proposal based on the feedback they had received. The WG has now held a total of five Member Informational Sessions and will present a final proposal to the full board in the coming months. The WG will also continue formal negotiations with the City of Austin with the goal to enact any agreed-upon changes during the 2025 legislative session. For background information on this topic, please refer to *AFRF News Issue #3*. For updates and calendar notices for future Member Informational Sessions, please see the Fund's website, including the new dedicated Plan Sustainability page at AFRFund.org/publications/plan-sustainability/.

Actuarial Matters

Experience Study | As a proactive measure to inform the development of a Voluntary FSRP, the AFRF Board decided to conduct an actuarial experience study one year in advance of the legal requirement. The Fund's actuary, Cheiron, presented the results of the study to the board in April. For accuracy, they recommended adding an explicit assumption for administrative expenses, separate from the investment return assumption. Based on actual Fund experience and Cheiron's future projections, they recommended a few minor assumption changes, including mortality rates. Cheiron recommended that no changes be made to the Fund's amortization method, cost method, or asset valuation method.

Valuation | Cheiron presented the valuation to the board in July, reporting that there had been no significant changes in the plan membership, provisions or investment strategy during the 2023 fiscal year.

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The State of the Fund

Investment Performance | Meketa reported a strong first quarter for 2024, with most major indexes up, led by US equities and impacted by the artificial intelligence boom. Fixed income categories were more muted or negative through early 2024 due to inflation, economics, and the response of the Federal Reserve. Second quarter returns were negative, resulting in a net positive but underperforming year-to-date investment return at the close of 2Q24.

IPPE Update | In August 2023, the board hired Callan as a third-party vendor to conduct the Fund's Investment Practices and Performance Evaluation in line with the requirements of Texas state law. The IPPE was presented to the board in draft form in April, then completed and submitted to the Pension Review Board in May along with the Fund's response. The overall findings indicated that all Fund processes and procedures are sufficient and consistent with industry best practices, the Fund is proactive toward fee optimization, and is performing well from a governance perspective.

PAS Software Update | AFRF has been making strong progress toward the implementation of their new Pension Administration System (PAS). Staff completed User Acceptance Testing (UAT) for the first set of software deliverables related to benefits calculations, employer transmittal files, and general system functionality, and have completed design review and UAT training for the second deliverable set related to payroll processes and correspondence. The third and final set of software designs is scheduled for review and testing in 2025 and will be followed by a period of parallel processing between the current and new systems. The project remains on track and within budget.

Depository Bank | In April, the board revisited the RFI for Depository Bank. At the time of the original RFI in 2023, no responsive banks were offering collateralized deposits, so the board decided to remain with Sunflower Bank until that requirement could be met. Frost Bank followed up in March to indicate that they were able to provide the requested collateralization and offered a preferable earnings credit rate and lower service charges. The board approved a motion to hire Frost Bank at their May meeting. The transition took place over the course of four months and was completed in mid-September.

Member Services

Considering Retirement? | Contact us for retirement benefit estimates or to schedule a benefits counseling session. Counseling can be conducted virtually or at the AFRF office.

State Tax Withholding | Effective January 1, 2025, AFRF will cease to withhold state taxes for payees who have relocated outside of Texas. This administrative change is due to constraints within the new pension administration software. If you are impacted by this change, please take appropriate action with your local tax office to ensure your tax obligations are met.

Trustee Election | Trustees of the AFRF board serve on a rotating term basis, with one trustee position up for election each year. This year, Vice Chair John Bass's position is up for election. John Bass, Richard Meyers and AJ Padilla have accepted nomination. The election period will run from Oct. 17 - Nov. 6 and will be hosted by an outside vendor, YesElections. Please check your mail and/or email for your voting materials, including biographies from each candidate.

Want More? | Following each publication, the AFRF staff has received feedback that the newsletters are very informative but leave our members wanting even more information! Our newsletter is intended to provide a high-level overview of the ongoing in the Fund. Our website provides thorough information about each topic covered in this newsletter, particularly in our Meeting Minutes. Use the months referenced in these overviews as a guide to locate your desired information.

Actuarial Matters, Continued

Valuation, continued from page 3 | In addition to the key valuation results included in the Annual Report (see page 2), Cheiron reported a Fund depletion date of 2062 under the Governmental Accounting Standards Board (GASB), further indicating the need for reform. The full Actuarial Valuation contains information on Fund assets, liabilities, and contributions, including identification and assessment of risk and stress-testing. The report can be viewed on AFRFund.org under the Publications menu.

Important Dates

September

30 | September Regular Board Meeting

October

15 | Deadline for October DROP Requests

17 | Trustee Election Opens

25 | October Regular Board Meeting

November

06 | Trustee Election Closes

11 | Office Closed for Veterans Day Holiday

15 | Deadline for November DROP Requests

22 | November Regular Board Meeting

22 | Trustee Election Results Certified

28-29 | Office Closed for Thanksgiving Holiday

December

16 | December Regular Board Meeting

15 | Deadline for December DROP Requests

24-25 | Office Closed for Christmas Holiday

January

01 | Office Closed for New Year's Day

15 | Deadline for January DROP Requests

20 | Office Closed for Martin Luther King Jr. Day

Updates to this calendar can be found on AFRFund.org.



Connect with Us

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