City of Lincoln, Nebraska
Police and Fire Pension
Funding Policy

APPENDIX B

I. Introduction

This funding policy pertains to the City of Lincoln, Nebraska ("City") Police and Fire Pension ("Pension") as described in Lincoln Municipal Code § 2.62.010, 2.65.010 and 2.66.010. The Pension Administrator sets the following guiding principles in the development of a comprehensive funding plan to maintain long-term sustainability, if needed:

- Shared responsibility among members and employer;
- Intergenerational equity;
- Preservation of the defined benefit plan.

II. Funding Goals

The objective of funding the Plan is to accumulate sufficient assets during a member's employment with the City to fully finance the benefits the member receives throughout retirement. In meeting this objective, the Pension Plan will strive to meet the following funding goals:

- To maintain a pattern of stable contribution rates as a percentage of member's payroll;
- To maintain an increasing funded ratio absent the impact of any changes to the assumptions or benefit provisions;
- To maintain adequate assets so that benefit payments can be paid to members and their beneficiaries as they become due.

III. Benchmarks

To track progress in achieving the previously outlined funding goals, the following benchmarks will be measured annually as part of the actuarial valuation with recognition that a single year's results may not be indicative of long-term trends.

Funded Ratio: The funded ratio, defined as the actuarial value of assets divided by the actuarial liability, should be increasing over time, before any adjustments for changes in benefits, actuarial methods, or actuarial assumptions.

City's Contribution: An Actuarial Valuation Report shall be prepared annually, as of the City's fiscal year-end date, to calculate the Actuarially Determined Employer Contribution for the fiscal year ending two years after the valuation date. For example, the Actuarially Determined Employer Contribution for the fiscal year September 1, 20XX+1 to August 31, 20XX+2 shall be based on metrics in the August 31, 20XX Actuarial Valuation Report. The Actuarial Valuation Report shall be based on the actuarial assumptions and methods, as approved by the Plan Administrator. The Actuarially Determined Employer Contribution Rate shall be the greater of the Employer Normal Cost Rate or the sum of the Employer Normal Cost rate and the UAL contribution rate. A negative amortization payment shall only be applied if the plan has been at least 110 percent funded for the current and

prior two years. The dollar amount of the Employer Contribution shall be the ADEC rate multiplied by the valuation payroll projected forward to the fiscal year under consideration, plus the actual administrative expenses for the fiscal year ending on the valuation date projected forward one year with the valuation's inflation assumption.

IV. Actuarial Methods and Assumptions

Actuarial Cost Method: The actuarial cost method is a mathematical budgeting procedure for allocating how the total present value of future benefits for current active and inactive members is allocated to each year of service, including past years. Due to the goal of stable contribution rates, the Plan Administrator has adopted the Entry Age Normal actuarial cost method.

Asset Smoothing Method: The method of valuing assets is intended to recognize a "smoothed" value of assets that is market related. Asset smoothing methods reduce the effect of short term volatility on contributions while still tracking the overall movement of the market value of assets by recognizing the effects of investment gains and losses over a period of years. The asset valuation method used to develop the actuarial value of assets first calculates the expected earnings on the prior year's market value of assets plus net cash flow (contributions minus benefit payments for the year) and then compares it the actual earnings on the market value of asses. The difference, positive or negative, is recognized equally over a five-year period.

Actuarial Assumptions: The actuarial assumptions used in the actuarial valuation shall be derived and proposed by the Plan's actuary in conformity with the applicable *Actuarial Standards of Practice* issued by the Actuarial Standards Board. The assumptions are intended to represent the best estimate of anticipated experience and are intended to be long-term in nature. In the development of actuarial assumptions, not only past experience but also trends, external economic forces, and future demographic and economic expectations shall be considered. A formal investigation into the actual experience of the Pension Plan shall be conducted by the actuary at least every five years and the results of the investigation used to form the basis of the actuary's recommendations for changes in the assumptions. In addition, the actual experience compared to the actuarial assumptions will be monitored each year in the annual actuarial valuation by including an analysis of the actuarial gain or loss.

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Amortization Policy: For the Actuarial Valuation Report prepared as of August 31, 2016, the amortization period of the Unfunded Actuarial Liability (UAL) shall be a 28-year closed term. This will be designated as the initial UAL base for subsequent valuations and will be amortized over the remaining years of the 30-year closed period set on August 31, 2014. For each Actuarial Valuation Report subsequent to August 31, 2016, annual net experience gains/losses will be amortized over a new, closed 20-year period. Subsequent plan amendments or changes in actuarial assumptions or methods that create a change in the UAL will be amortized over a demographically appropriate time period selected by the Plan Administrator at the time that the change is reflected in the annual actuarial valuation.

If the valuation shows a surplus, i.e., funded ratio above 100%, the prior amortization bases will be eliminated and one base equal to the amount of surplus shall be established. The amortization period of a surplus shall be a 20-year open period.

The amortization payment on each UAL base will be calculated as a level percent of valuation payroll using the actuarial assumption for future payroll growth. Such calculation is consistent with the development of the normal cost rate and is intended to serve as a method to provide stability to the actuarial contribution rate.

Risk Control: The Plan Administrator will carefully monitor the key risk measures of funding the system and shall consider steps to mitigate risk, particularly as the funded ratio increases. Risk mitigation may involve such things as a reduction in the assumed rate of investment return, review of asset allocation with a goal of reducing the standard deviation of the portfolio return, establishment of a contribution rate stabilization reserve, and other strategies identified by the Plan Administrator.

V. Funding Policy Review

The Plan Administrator may periodically conduct special studies to provide insight into whether the goals and objectives established in this Policy are being met. These special studies may include asset liability studies, projection modeling studies, and sensitivity analysis of key risk factors. These special studies may be performed at the Plan Administrator's discretion.

It is recognized that this funding policy may need to be amended in the future as the funding of the Plan is a dynamic process which is dependent on a number of variables. Therefore, the funding policy will be reviewed and amended as necessary by the Plan Administrator, but not less frequently than every five years following the actuarial experience study.