Volume 47, March 2012

PENSION PRESS

Special Edition

The Newsletter of the Houston Municipal Employees Pension System

www.hmeps.org

An Update From the Chairman

Dear Plan Participants:

Sherry Mose
Chairman

I am sure many of you have been following recent media coverage of the activities of the City of Houston's Long Range Financial Management Task Force (Task Force) that Mayor Annise Parker and the City Council created last year to analyze and describe options for the City to meet its General Fund financial obligations over the next 30 years.

As you may know, the Task Force delivered its final report to the Mayor, and presented it to City Council on Wednesday (Feb. 8). While the Task Force's mission explicitly states it is not to recommend, endorse or champion any single option, in fact the report unfairly and inaccurately targets pensions as a solution to the City's financial problems. Unfortunately, many Task Force members argued to give the City control of the pension systems. This can be seen in both their report and subsequent editorials published in the local newspaper.

In response, the six Task Force members representing the pension systems and union beneficiaries submitted a Minority Report, which urges a comprehensive approach to reducing the City's budget. In the Minority Report, we remind everyone that pensions are set up as trusts with strict oversight and controls, which assures protection of pension assets. In the past, these funds were not protected, which is why public plans became separate systems with independent governance. Our response to the City control issue and to other pension misconceptions is set forth in the Minority Report, which can be viewed on our website at www.hmeps.org.

We want to assure you that this task force has no official authority to enact any changes to the benefit plans for City of Houston municipal workers. This was an advisory panel only, and it has no statutory authority to change any pension system, including HMEPS. Changes to the HMEPS plan can occur only through

(Continued on Page 2)

Stay In Touch – HMEPS Needs Your Email Address!

HMEPS needs your email address so that we can keep you informed and updated on pension matters quickly and effectively. For fast and easy submission, go to our website at:

www.hmeps.org

Click the "Stay Connected!" box on the home page and follow the simple instructions.

HMEPS will use your email address only for general communication and not for providing any personal or individualized information. We do not share personal email addresses with third parties. **Thank you!**

Letter from the Chairman (Continued from page 1)

negotiated agreements in the Meet and Confer process between the HMEPS Board and the City, or in the State Legislature.

City officials recently stated that the pension systems do not provide them with sufficient information to do their financial planning. All raw data – employee work and pay history – comes directly from the City, and all rules for calculating pension benefits are open and public. Also, the City is regularly provided with detailed aggregate information about all pension benefits. What the City really is seeking is detailed information about pension benefits and DROP account activity on an individual basis. But we firmly believe we are obligated to comply with all legally required privacy and confidentiality conditions that protect participant information.

In our continued effort to assure a balanced discussion on pension matters, we will continue to communicate with city and state leaders about pension issues and to monitor any and all efforts regarding pensions.

We also want to enhance our communications with you. A critical part of keeping you informed is the ability to reach you quickly and effectively, and the best way to do that is through email. We urge you to provide us your email address so that we can keep you updated and informed. Please visit www.hmeps.org and submit your email address through the link on the home page. It's fast, easy and will help us be more effective in reaching you with important updates.

As always, the HMEPS Board and staff remain committed to protecting and strengthening the System for its participants, now and in the future.

Sincerely,

Sherry Mose

It's Time to Stay Informed and Get Involved

Lonnie Vara
HMEPS Secretary and Trustee

Recently, members have raised concerns over the national and local attention that has been focused on public pensions. Our staff and trustees have worked hard to bring facts and information to stakeholders and elected officials at the local, state and national level, and to counter the many misleading stories and attacks on public pension plans. You can make a big difference by advocating and making your opinions and concerns known at every opportunity. Our strength is in our numbers and staying informed and educated.

Here are two ways you can get involved and stay informed:

First, join the Association of Retired Houston Municipal Employees (ARHME). ARHME is a new organization of fellow workers and retirees. Its purpose is to inform and educate City municipal retirees about pension, health and other pertinent issues. It is also a means to stay connected to one another. These goals are very important, as we must always be ready to protect and preserve our municipal retirement benefits. To join ARHME, go to their website (www.arhme.net) and complete a membership application or contact ARHME at 713-646-6729 or at P.O. Box 40354, Houston, Texas 77240.

Second, join Texans for Secure Retirement (TSR). TSR was created to coordinate the efforts of the many local pensions systems and the numerous public employees at the state, county and local levels. TSR will educate the general public about the value and need of the public sector's defined benefit plans and fight the misinformation that is being given out by such groups as the Texans for Public Pension Reform, which was formed with the purpose of removing all Texas government employees from defined benefit plans, like ours, to plans similar to 401(k)s. You can join and learn more about TSR by visiting their website (www.texansr.com).

By bringing all of our strengths to bear, we can help educate and turn back the misinformation campaigns and focus on providing greater retirement security for City employees.

Sincerely,

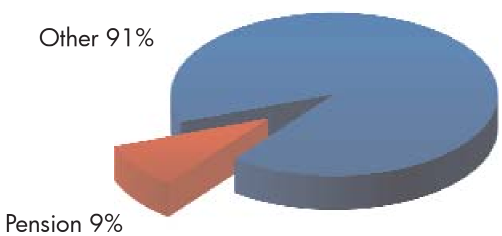
Lonnie Vara
HMEPS Secretary and Trustee – Retiree position

Summary of the Minority Report Responses to the City's Task Force Report

Summary of key pension-related items in the Minority Report:

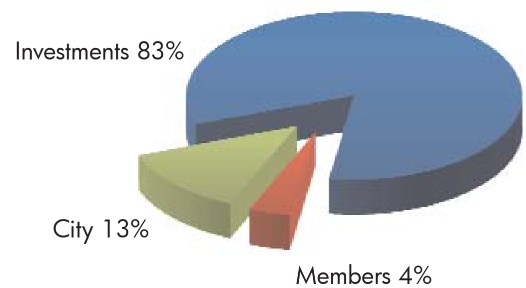
- We fully support the goal of addressing core, long-term financial problems faced by the City of Houston.
- The identification of pensions as the source of these problems is misguided. Pension contributions make up 9% of the General Fund budget in fiscal year 2012, and even less when the entire City budget is considered.
- The City is ignoring the true underlying cause of its problems – which is its own institutional tendency to take on long term obligations (such as its $13.1 billion debt overall) without adequate planning for how to pay for these obligations.
- Further sacrifices by City employees would do little to solve this underlying problem.
- 401(k) style approaches to retirement financing are not cheaper than the defined benefit (DB) approach, when properly compared on an apples-to-apples basis. Switches to 401(k) style accounts are often used to hide drastic cuts in benefits.

FY 2012 City General Fund Budgeted Cost Breakdown



- The City argues that it doesn't have enough information from the pensions. But in fact the rules for calculating all benefits are completely open and public, and the underlying payroll data comes directly from the City. In addition, substantial aggregate data is regularly provided to the City. The City wants information about individual pension and DROP activity. Not only is individualized information not meaningful for long-term planning, but HMEPS must assure that legally required privacy and confidentiality conditions be absolutely respected.
- Given the City's history, the notion that the City should have "more control" over the pensions systems and their assets is illogical. In any case, pensions are set up as trusts with strict oversight and controls to prevent governments from raiding the assets to pay for other projects. This has happened in the past, which is why public plans are now separate systems with independent governance, while still including City appointees.

Sources of Funds for Houston Pensions FY 2011



For the full Minority Report on the Long-Range Financial Management Task Force, go to http://www.hmeps.org and click on "Update On the City's Financial Management Task Force." We encourage you to read it. You should encourage others, including your elected state and local leaders, to read it as well for a balanced perspective.

Visit the HMEPS Website for these and other reports:

The following reports that are referred to in this Special Edition of the *Pension Press* are available on the HMEPS website at www.hmeps.org:

- ☑ **The Minority Report on the Long Range Financial Management Task Force**
- ☑ **City of Houston Task Force Report**
- ☑ **HMEPS Comprehensive Annual Financial Report for the Year Ending June 30, 2011**
- ☑ **HMEPS 2011 Report to Participants**
- ☑ **Report from the Center for State & Local Government Excellence**

HMEPS Investments

Assets as of 6/30/11: $2,129,441,342
Investment return for FY 2011: 22.17%
Assumed Rate of Return: 8.5%

HMEPS is well-positioned to deliver secure benefits to its members and value to taxpayers for many years to come. This is due in large part to its robust, well-managed investment portfolio. As of 6/30/11 HMEPS has approximately $2.1 billion in assets. Over the last 10 years, its investments have performed very strongly compared to other public funds. The System's 10-year annualized return is 7.75 percent compared to the median public fund's return of 5.59 percent. The System's twenty-year return is 9.26 percent.

Investments Overview:

- Investment returns are critical to the financial health of the system
- Investment returns have a major effect on the City's contribution rate
- Increases in HMEPS' investment performance over the assumed rate reduce the City's required contribution rate
- Reduced volatility in HMEPS' investment performance reduces volatility in the City's required contribution rate

Investment Portfolio:

- 8 Asset Classes
- 52 Investment Managers (15% MWB)
- 99 Investment Portfolios

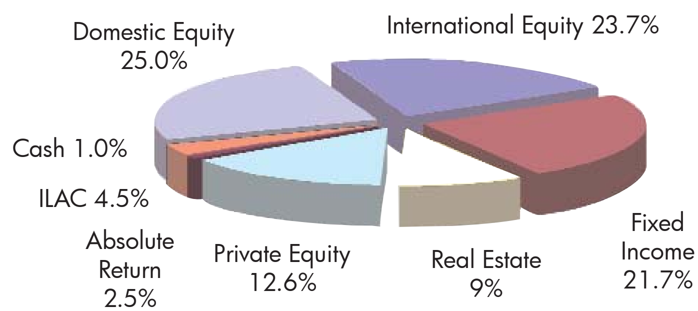
Highlights:

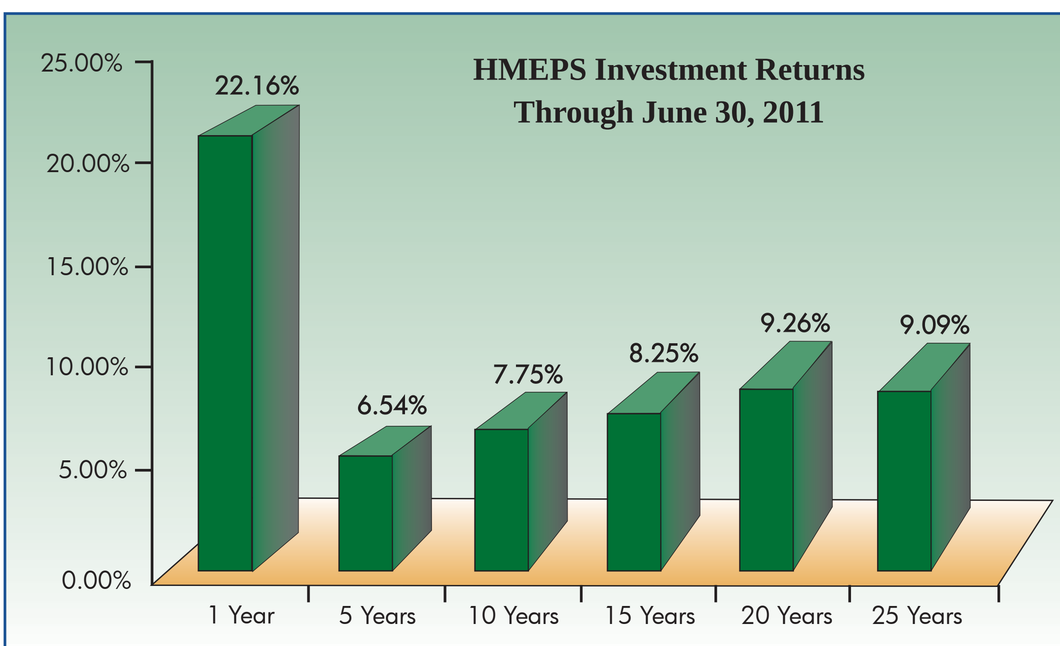
- Portfolio is designed with a long-term view
- Broad diversification reduces volatility

Objectives:

- Maximize the safety of promised benefits
- Minimize the cost of funding the benefits

Asset Allocation as of 6/30/2011:





The Good News About Pensions

by Rhonda Smith, Executive Director

Rhonda Smith
Executive Director

HMEPS is in a strong position today because of early, proactive steps taken by its leadership to work with the City to secure the System's long-term viability. While many other pension systems today face serious challenges to maintaining their long-term viability, HMEPS has been singled out as an "inspiration" by the Ft. Worth Star Telegram for resolving such challenges, and was identified by the Center for State & Local Government Excellence as one of five pension systems in the U.S. that has made reforms that make them "more fiscally sustainable while continuing to provide retirement security to their members."

HMEPS has already taken significant steps to secure the pension plan for the long term. Nearly a decade ago, HMEPS faced a long-term funding liability similar to those confronting some public pension systems today. By working together with the City of Houston, HMEPS took concrete steps to shore up its liability, resulting in a stronger system that is the bedrock upon which City employees have built a secure and hard-earned retirement. In fact, HMEPS began working proactively to improve the system's funded status in 2004, long before the current outcry over public pensions.

Working with the City through the Meet and Confer process, HMEPS made the tough but necessary choices, including cutting future benefits by over $850 million, implementing increases in employee contributions and retirement age, and providing the City budgetary flexibility to weather the economic downturn. Thanks to proactive leadership, HMEPS now has over $2 billion in assets, has substantially increased its funding and is strongly positioned, both for the short and long term.

- **City of Houston municipal employees receive a modest retirement pension.** A common misconception is that all pensions are too lucrative or "gold-plated" and being paid to folks who exit the workplace in their 50s. But that is not a fair or accurate representation of the hard-working employees who serve the City. At HMEPS, those employees who are hired after 2008 are not eligible for full retirement until age 62. The average HMEPS retiree is 67 and receives an annual benefit of less than $23,000 a year – hardly a gold-plated pension in today's world.
- **City municipal employees share in the financing of their pension.** A significant number of current HMEPS members contribute 5 percent of their wages to help fund their pension. These employee contributions, along with investment returns, comprise the majority of public pension fund revenues.
- **Retirement systems remain a small portion of the city's budget.** The city pensions are not paid out of general operating revenues, but instead, from trusts to which the employees and the City contributed while they were working. Legislators and plan sponsors often focus on pension contributions as a percent of payroll. Pension contributions as a percent of budgets, however, provide a broader framework for projecting how public pensions will affect local activities. An analysis of the City's 2011 annual financial report indicates that contributions to HMEPS represent 5.4 percent of the City's total budget.
- **Long-term investment returns of public funds continue to exceed expectations.** In ordinary times, over 2/3 of the pension funding comes from returns on the system's investments, which are professionally managed, and which returned over 22% last fiscal year. HMEPS has over $2 billion in assets and is a long-term investor with a well diversified investment portfolio and a time horizon that lasts over decades. HMEPS, while not immune to the effects of the recession, has weathered the storm better than most public pension systems in part because of sound management of its assets. Over the ten-year period ending June 30, 2011, HMEPS' investment performance is in the top one percent of public funds.

We all know that governments are facing challenges, and retirement plans like HMEPS are ready to work with them. Instead of blaming the City's fiscal woes on pension systems, the City's overall debt service, which has been passed on from administration to administration until it has reached epic proportions, should be the more immediate concern. Public employees did not create the problem, but they have worked to be part of a reasonable and fair solution.

You and Your Pension: A Powerful Combination *by Steve Waas, CFP®, EA*

Steve Waas
Financial Counselor

If you have been following the news, you have probably noticed that there has been a growing movement both nationally and in the state of Texas to eliminate DB plans and replace them with 401(k)-style defined contribution (DC) plans that instead restrict members to individual separate accounts. This campaign will probably accelerate over the next couple of years.

Should you care?

YES.

It is common for opponents of DB plans to point to private sector retirement plans as a model. In the private sector, DB plans have been increasingly replaced with DC plans. Often the end result has been to cut overall compensation in ways that were not well understood by the affected employees. This is because comparing DB and DC benefits is a very complex task.

To see this, consider a typical HMEPS retiree. The average annual annuity for an HMEPS retiree is slightly less than $23,000 per year. Without a DB plan, how much savings would a 65 year old worker need to be able to generate this income for the rest of his life? About $550,000.

Over a 30 year career, this worker would need to save at least 26% of his salary, each and every year, in order to end up with this much savings. This assumes he earns, when near retirement, about $35,000 a year and that he invests very successfully.

Considering that the median 401(k) match in the private sector is about 2%, it's not hard to see why many people have fallen so far behind in their retirement plans – often not realizing it until they want to retire.

Switching from DB to DC usually involves providing a "lump sum" of money to the participant. Presumably, this represents the value of the forgone DB benefit. Lump sums seem to be irresistible to people, regardless of what it costs them. Many companies in the 1990s exploited this common tendency while quietly cutting pension obligations.

One study of a huge lump sum payout program from a pension plan in 1992 showed that thousands of workers, by taking immediate lump sums instead of future monthly payouts, effectively turned down guaranteed rates of return of nearly 20 percent per year. The researchers calculated that this translated into a net transfer of $1.7 billion from the employees to the employer.

DB pensions are often viewed by critics as an excessively "expensive" component of compensation. But the simple fact is that retirement is expensive. Instead of coming to terms with this fact, Americans are cycling through various alternatives in the hopes that one of them will somehow render retirement cheap. Here are some of these "solutions":

- ***Rely entirely upon 401(k)-style accounts, since they are a much cheaper way to save for retirement.*** But a closer look reveals that these accounts are not cheaper and have left millions of Americans with drastically underfunded retirement accounts. (To learn more, see "Why Pensions Work" at www.hmeps.org and click on Resources: Learn More About Pension Issues.)
- ***All we need to do is raise retirement ages, since life expectancies have risen.*** Raising retirement ages may be appropriate in some cases, but this is not the general solution that many people seem to think it is. First, while life expectancies have indeed increased, we must also recognize that health conditions vary significantly among older workers. Retirement is not always a matter of choice. Furthermore, while many people have nice, indoor jobs in air conditioned offices, society still depends on millions of workers in physically demanding jobs such as hauling garbage, fixing roads, fighting fires and chasing criminals. Expecting all of these workers to continue these jobs into their 60s may not be realistic.

As with any program or system, unexpected challenges can arise. When necessary, state and local governments have taken steps to modify the design of their plans, in order to accommodate changing circumstances and needs. HMEPS has taken concrete steps to improve the pension system and has continued to pursue responsible pension reform.

At the end of the day, saving for retirement is both necessary and expensive. This will be true regardless of the approach. A reasonably structured DB pension remains a highly efficient way to deliver the core financing that people need for retirement.

If our common goal is achieving adequate retirement security, then we need to be concerned and vigilant about the increased efforts to replace traditional defined benefit pension plans with 401(k)-style plans. What's at stake is your retirement security and your ability to live the future you have earned.

Steve Waas is a Certified Financial Planner and the HMEPS Financial Counselor. Steve is available for individual meetings with participants and also discusses financial topics in our newsletters to help participants better understand these important issues.

The information contained herein is general in nature and is not intended as legal, tax, or investment advice, and should not be used in any actual transaction without the advice and guidance of a professional tax advisor who is familiar with all the relevant facts. HMEPS assumes no obligation to inform any person of any changes in the tax law or other factors that could affect the information contained herein.

Retirements – 4th Quarter 2011

Administration & Regulatory Affairs

Joseph, Shelton

Aviation

Bernardo, Davila
Edwards, James
Johnson, Leroy
Spradling, Joseph

Fleet Management

Contreras, Andrew
Evans, Hansel
Morgan, Enoch

General Services

Jackson, Lugene

Health & Human Services

Pitts, Kate

Library

Goodman, Marjorie

Public Works & Engineering

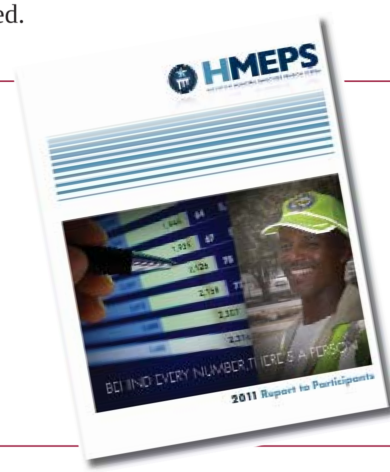
Adams, Clinton
Davis, Jr., Hezekiah

Solid Waste Management

Smith, Larry

Notice on Newsletter Sections "Retirements" and "In Remembrance"

Two newsletter sections, "Retirements" and "In Remembrance," have had to be reworked to take into account changes in Texas law. The Retirement section now lists names and departments of those retiring participants who have indicated on their retirement application that they wished to have an announcement of their retirement included.



Annual Statements and Reports to Participants Mailed

Annual Pension Statements (active employees) and DROP Statements (participants with a DROP balance as of 12/31/11) were mailed in mid-February. Each packet mailed also contained the 2011 Report to Participants. We hope participants enjoy reading the Report.

If you did not receive your statement(s), please call the HMEPS office.

Pension Payment Schedules March to July 2012

The following are the dates pension benefit checks will be mailed in the months ahead. The schedule will be strictly adhered to.

- **Tuesday, March 27**
- **Wednesday, April 25**
- **Friday, May 25**
- **Tuesday, June 26**

Direct deposits (ACH) will be deposited on the last business day of each month, as follows:

- **Friday, March 30**
- **Monday, April 30**
- **Thursday, May 31**
- **Friday, June 29**

If you are interested in direct deposit of your pension benefit, please call our office at 713-595-0100.

HMEPS Website Offers Access to Annual Reports, Investment Data and More

Did you know the HMEPS website has publications available for viewing? Annual Reports, Actuarial Valuations, past newsletters and more are available at the click of your mouse.

Here is how to access the information:

1. Go to the HMEPS website at www.hmeps.org.
2. Select the link that is titled "Publications" and scroll down to the type of publication you are seeking.
3. Click on the icon and the selected publication will open with Adobe Acrobat. Adobe Acrobat is available for free on the website and is a handy tool for opening many documents online.

If you need assistance, please call the HMEPS office at 713-595-0100.

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PENSION PRESS

Rhonda Smith, Executive Director
Peter Koops, Communications Specialist

Thanks to the HMEPS staff for their contributions to the ongoing success of the *Pension Press.*

NEWSLETTER CONTENT

The material contained in this newsletter is intended to provide you with important information about your pension participation. The content cannot be taken as the basis of any contractual rights between HMEPS and its participants. If there is a question of interpretation, retirement laws are the final authority.

HMEPS CONTACT INFORMATION

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Toll Free: 800-858-1450
Fax: 713-650-1961

HMEPS Website:

www.hmeps.org