

**State Pension Review Board
Actuarial Committee Meeting
Minutes
June 17, 2014**

1. Meeting called to order

The third meeting of 2014 of the State Pension Review Board (PRB) Actuarial Committee was called to order by Chair Bob May on Tuesday, June 17, 2014, at 10:00 a.m. at the Employees Retirement System of Texas (ERS) in Austin, Texas.

2. Roll call of Committee members

Board Members Present:

Robert M. May
Andrew W. Cable
Keith W. Brainard

3. Approval of the April 22, 2014 Committee meeting minutes

Mr. May entertained a motion to suspend the reading of the Minutes of the PRB Actuarial Committee meeting held April 22, 2014.

Motion made by Mr. Brainard, seconded by Mr. Cable that the PRB Actuarial Committee suspend the reading of the minutes of its meeting held on April 22, 2014.

MOTION CARRIED UNANIMOUSLY

4. Discuss and consider the study of the financial health of public retirement systems in the state as required by Section 7 of House Bill 13 (83rd Texas Legislature)

The PRB Guidelines for Actuarial Soundness has been the minimum best standard and best practice the Board has recommended for funding a defined benefit public retirement system. Mr. Hanson noted that part of the information included in the reports utilizes the Guidelines. The financial health study calls on the Board to determine each retirement systems' ability to meet its long-term obligations while taking into account the contributions made to, the benefits paid by, and the investments made by the retirement system. The PRB has used the Guidelines as a minimum standard since 1984, and staff plans to move forward with the idea that anything over a 40-year amortization period, the minimum requirement to be considered actuarially sound, would not be deemed as a sufficient funding arrangement to meet a system's long term obligations.

Mr. May suggested a shorter amortization period than 40 years, and proposed revising the Guidelines after this session of the Legislature and reviewing them as a separate project next year.

Mr. Hanson reviewed the June, 2014 Actuarial Valuations Report, and noted that a Plan Status column has been added. The Report is presented to include the actuarial information as it currently stands and to make sure it is in readable and usable format. Three statuses have been identified: active, closed, and frozen. Mr. Hanson noted that the status for the plan type changes when reviewing and comparing funded ratios, cash flows, and demographics. A question presented to the Committee was whether or not the PRB should continue to differentiate the plans that are no longer active and within the two categories of closed or frozen.

Mr. May suggested creating a fourth pay-as-you-go status column for the Judicial Retirement System of Texas Plan One.

Mr. Hanson stated that a challenge with the study is being as current as possible with the information. There are systems currently evaluating changes and that have implemented changes that have not been reflected in the report. Mr. Hanson noted there will be a period of time between the preliminary report and the final report for systems to comment, and stated that goal of the PRB is to accurately reflect the most current and active information for every system in the December 31st report to the Legislature.

Chris Bucknall, Texas County and District Retirement System (TCDRS), commented that many times an overfunded plan will have an open 30-year amortization period, and he recommended using a zero to avoid

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confusion. He stated that for TCDRS and Texas Municipal Retirement System (TMRS), there are various categories, and he would encourage letting them list the number of plans by amortization period and customizing them.

Mr. Hanson recommended footnoting TCDRS and TMRS in the report as there will be additional details on the two systems, and suggested identifying the two systems as multi-employer systems, making sure that if there is an aggregate amortization period that it is reflected in the list.

Mr. Hanson reviewed the Preliminary Analysis of Historical Information for the Study of the Financial Health of Public Retirement Systems which concludes the staff's research on the information gathered on each of the state retirement systems. The most important factor staff has identified in meeting a system's long-term obligations based on the amortization period is the contribution policy. Systems that have received insufficient contribution levels over a long period of time have experienced a decline in their financial health. Mr. Hanson stated that over the last ten years, the investment performance has varied significantly from plan to plan; however, that has not been the case for plans with amortization periods under 25 years. In reference to non-investment cash flow, the average cash flow is within reasonable ranges for most systems overall. For a few systems however, non-investment cash flow as a percent of total net assets is less than 5% and may be impacting their financial health. In reference to plan demographics, the ratio of active to retired members has declined since 2000 with the decline being steepest in systems with amortization periods of greater than 40 years. With benefit policy decisions, there is a higher percentage of benefit enhancements since 1995, although there are a percentage of systems with amortization periods below 25 years that have also increased benefit enhancements. Mr. Hanson noted that overall, funded ratios have declined since 2000, and the asset to liability growth has been lowest for systems with amortization periods over 40 years.

Mr. Hanson stated that a financial history review was conducted which compared systems' gross and net rolling one, three and ten-year rates of return, and noted that the rates of return were calculated based on the internal rate of return formula. Mr. Hanson mentioned that staff identified the contribution history review as the strongest correlation to a system's current amortization period and the biggest factor on a systems ability to meet its long-term obligations is the contribution policy.

Mr. Brainard mentioned it is worth noting that the most mature systems are those with the fewest active annuitants and with the longest amortization periods. He suggested including in the report a description of the structure that governs contributions and benefits including constitutional, statutory, and administrative. He stated that it would be helpful to notify readers of the report what restraints or requirements are in place with regard to making overall contributions. He commented that it is notable that the TLFFRA plans are substantially underperforming in comparison to other systems.

Mr. Stacy noted that TLFFRA represents almost half of the total public systems in the state yet less than one percent of the assets.

Mr. Hanson stated that a challenge for staff in regards to some of the TLFFRA systems is that for many years they provided their financial information to the city audit, and there have been instances where the PRB may not have received information that is as current for some of the smaller systems. He mentioned that staff would like to incorporate their actual reports to the PRB, and stated that the PRB uses a particular investment return report and wanted to make certain that the systems are afforded the ability to provide this information.

Mr. Hanson reviewed the Public Retirement System Sponsor Financial Information.

Mr. Brainard stated that he found the information to be very useful, and suggested adding a column that would divide one of the shortfall amounts into one of the other columns to create a percentage. He also suggested combining the plans sponsors in a separate table.

Mr. Hanson noted that it may be helpful to primarily focus on systems that are currently over 40 years and have a 40 year shortfall, and combine them by plan sponsors.

In reference to the Preliminary Analysis of Historical Information, Jennifer Jones, Employees Retirement System of Texas (ERS), asked if it would be possible to make a broad statement about whether the benefit enhancements were pre-funded by the plan sponsors.

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Mr. Hanson stated that there were instances where there were a limited number of contributions that were raised in conjunction with the benefit increase, but it was the smaller percentage.

Mr. Hanson reviewed the draft outline of the Financial Health Study, and stated that the outline will evolve as the study is drafted.

Mr. Hanson noted that a requirement of the study is to include recommendations regarding how a system may mitigate its risk of not meeting its long-term obligations. After staff review, past discussion, and other recommendations, staff put together a combined list of different items. The items are intended solely for discussion purposes at this time, and are not official recommendations. Mr. Hanson reiterated an earlier comment from Judge Cable stating that legislation could be created from this report, and that any recommendation included shall be thought of in that context.

Mr. Brainard noted that earlier in the year, the state of Tennessee passed a bill requiring local retirement systems to pay their full annual required contribution starting in six years, or the state has the authority to make a full payment for them. He suggested mentioning this concept in the report and receiving feedback.

Chris Bucknall stated that it is important to look at lowering benefits, benefit adequacy, and whether or not there is social security coverage.

Mr. May noted that the concept of benefit adequacy is difficult because it is subjective. What might be adequate to one individual may not be adequate to another.

Mr. Brainard noted that he views benefit adequacy as a process, and that the plan sponsor should consider what a typical employee is likely to get out of the plan they are providing.

In response to an audience member's question concerning how the PRB intends to respond to inquiries from the media at the time the preliminary report is released, Mr. May suggested bringing this question in front of the full Board at the August 28th meeting.

Mr. Hanson reviewed a sample Investment Returns and Assumptions Report and noted that the PRB has received figures from a few of the systems, and have put together a draft report that will eventually need to be produced for the legislature as this is a new reporting requirement for all plans.

Mr. Brainard noted that investment returns are commonly misunderstood and the reaction of most readers tends to be to look at one or more systems and see how they compare to everyone else on the list without understanding the nuances of investment management. He suggested the board consider presenting information that is grouped by the size of the fund, the municipal state, TLFFRA, and other characteristics related to funding level. He further noted that a raw listing of investment returns by system can lead to bad outcomes.

Mr. May stated that it is misleading to talk about TMRS and TCDRS as one system, and his preference would be to show key information for each city and each county in the report.

Chris Bucknall suggested having all the systems not only put the amortization period down, but also note if it is closed, open, or a fixed rate plan as the numbers are so different.

Mr. Hanson reviewed the final chart in the packet, a contribution rate and amortization chart and stated that the overall sense from the committee members is to keep the data sets smaller for the preliminary report.

5. Date and location of next Committee meeting – Thursday, August 14, 2014, Austin, Texas

6. Adjournment

Chair May thanked the Committee and the audience for their participation at the meeting. With the business of the Committee completed, Chair May adjourned the meeting at 12:30 p.m.

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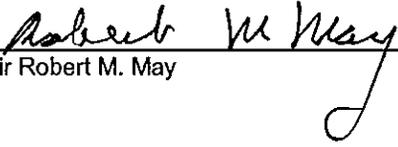
In Attendance:

Staff:

Chris Hanson
Daniel Moore
Reece Freeman
Bryan Burnham
Anne Benites

Guests:

Steve Waas, Houston Employees Municipal Pension System
Lon Craft, Texas Municipal Police Association
John Lawson, Houston Police Officers' Pension System
Leslee Hardy, Texas Municipal Retirement System
Eloise Raphael, Houston Firefighters' Relief and Retirement Fund
David Stacy, Midland Firemen's Relief and Retirement Fund
Katy Fallon, Legislative Budget Board
Chris Bucknall, Texas County and District Retirement System
Jennifer Jones, Employees Retirement System


Chair Robert M. May