BURLINGTON RETIREMENT BOARD
REMOTE MEETING WITH CALL-IN
BURLINGTON, VERMONT
MINUTES OF MEETING
DRAFT
February 12, 2024

MEMBERS PRESENT:
Robert Hooper (Chair)
Munir Kasti (Vice Chair)
Patrick Robins
Tom Chenette
Kyle Blake
Katherine Schad
Matt Dow

MEMBERS ABSENT:
David Mount

OTHERS PRESENT:
Hayley McClenahan
Darlene Bayko
Lynn Reagan
Richard Carey
Kate Pizzi
Chris Rowlins
Rob Lessard
Steve Lemanski

1.0 CALL TO ORDER
Robert Hooper called the Retirement Board meeting to order at 9:30 AM.

MOTION by Munir Kasti, SECOND by Kyle Blake, to adopt the agenda.

VOTING: unanimous; motion carries.

2.0 PUBLIC FORUM (VERBAL)
2.01 Verbal Comments
None.

3.0 APPROVE MINUTES

3.1 January 22, 2024

MOTION by Patrick Robins, SECOND by Kyle Blake, to approve the minutes of January 22, 2024 as presented.

VOTING: unanimous; motion carries.

4.0 ADMINISTRATIVE UPDATE

4.1 Administrative Update

Chief Administrative Officer Schad noted that this meeting is occurring a week early because an item that the BERS Board needs to discuss (the FY23 Valuation Report) has implications for the City's financial audit, which must be taken up by the Board of Finance next week. She noted that because this meeting is occurring a week early, the February retirement and return of contribution approvals were not yet ready to put on the agenda, and so those will also be up for approval during the March BERS meeting.

Assistant Director of Finance Bayko spoke about statistics that were requested at the BERS Board's January meeting. She noted that there are currently 879 retirees within the system, 50 of whom have a monthly payment of under $100 and 40 of whom have a monthly payment between $100 and $200. Mr. Hooper noted that they had requested these statistics to determine how many smaller payments are being issued from the system, given that there could be cost savings associated with issuing checks on a less frequent basis for smaller payments. He said that they could put this item on a future agenda for further consideration.

Assistant City Attorney McClenahan noted that this Board had had a question about the feasibility of purchase of service credit, and asked whether there has been an update from other City staff. Chief Administrative Officer Schad noted that she and the City's actuaries determined that it is possible but that it is not currently in the City's retirement plan and would need to be negotiated with the unions and also incorporated into an ordinance amendment, were the City to pursue this policy.

5.0 FIDUCIENT

5.1 Investment Portfolio and Performance Update as of 01/31/2024

Ms. Pizzi noted that one impact of moving this meeting up one week is that Fiducient's finalized January numbers are not yet available, though they have preliminary numbers to review at this juncture. She provided an update of the BERS portfolio's balances as of the end of January, noting that the portfolio stood at approximately $234 million as of the end of that month. She said that this is very similar to numbers as of the end of December, and that values are up approximately 0.1%. She said that this is largely due to many asset classes posting negative returns in January, except for U.S. large cap stocks. She spoke briefly about some of the major headwinds for January.

Ms. Pizzi spoke about current allocations for the portfolio, noting 25% of the allocating in fixed income, 75% in equities (42.7% in domestic equities and 27.5% in global equities), with some lingering real assets in the UBS Trumbull Property Fund. She noted that the portfolio is slightly overweight in the domestic equity allocation, but that is to balance the underweight in alternative/real assets, since they are in the full redemption queue for Trumbull.

5.2 Fiducient's Asset Allocation Modeling & Portfolio Implications for BERS

Ms. Pizzi said that at the last BERS meeting, in January, Fiducient's Chief Investment Officer presented on Fiducient's outlook for 2024. She said that two key points from that presentation were the increased expectations around future returns in the long-term for fixed-income assets, given the restoration of higher yields seen in 2023, and backing off expectations for global equities in the long-term. She said that one impact of moving this meeting up one week is that Fiducient's finalized January numbers are not yet available, though they have preliminary numbers to review at this juncture.

Mr. Rowlins began by briefly speaking about the capital market assumptions. He said that as part of the fiduciary governance calendar, one of the topics is this deeper dive into capital market assumptions and implications that they may have for the BERS portfolio. He showed the 2024-2033 Ten-Year Outlook, breaking it down into the fixed income, global equity, and real assets & alternatives classes, and the more granular subcategories within each of those asset classes. He noted that one of the building blocks of assumptions for the outlook is inflation, and spoke about how Fiducient produces its assumptions, given the volatility seen in the last two years around inflation. He noted that when looking at the yields on nominal bonds, the market is anticipating a 2.4% median inflation over the next ten years, which is what they're using for their assumption. He noted that the restoration of higher yields has led to higher projected performance for fixed-income assets. He noted that projections for U.S. and international equities are flat-to-falling, given higher geopolitical volatility outside the U.S. He noted higher return projections for real assets and alternatives. Ms. Pizzi added that the risk premium that has historically existed within the equity market when compared to the fixed-income market has decreased significantly this year, given the increased expectations for fixed income assets and decreased expectations for equity assets. She said that from a portfolio perspective, the same level of expected return can be achieved by utilizing more bonds and taking less risk in the portfolio. Mr. Rowlins spoke about the larger role that fixed-income could play in the portfolio, given higher bond yields, and said that the weighting of fixed-income is one major topic for today's discussion.

Ms. Pizzi spoke in more detail about the asset allocation analysis Fiducient conducted using the above capital market assumptions, noting that the overall goal is to ensure that the BERS portfolio is strong and structured to support its pension liabilities. She noted that the portfolio is currently generating an expected return of 7.9%, which is well in excess of the current discount rate of 7.1%. She noted that outperforming the discount rate increases the likelihood that the portfolio will generate a return in line with or above the expected discount rate. She presented an alternative allocation, Observation Mix A, which utilizes the different asset classes to maximize the potential return and minimize the potential risk. She said that this alternative increases fixed-income by 2% and removing it from the private real estate target (given that this is already underweight). She said that they are also recommending pulling back slightly on international equities and redistributing it to U.S. equities. She said that this has a minimal impact on the expected return, but decreases risk to the portfolio. She also spoke about Observation Mix C, which increases the allocation to fixed income similarly to Observation Mix A, but also moves allocation from private real estate to public real estate, which does not impact the expected rate of return but increases the risk/volatility slightly. Mr. Kasti asked about whether any analysis was conducted to show how this ultimately closes the unfunded liability gap that the pension currently has, and Ms. Pizzi replied that the goal of this is to ensure that the portfolio performance is in line with the actuarial rate of return assumption of 7.1%, and anything in excess of that will be able to close that unfunded liability gap over time. She said that as long as contributions are being made at the actuarially recommended rate, and that 7.1% rate of return is achieved, then the pension will get to that fully funded position over time. Mr. Lemanski noted that they will also speak to this in more detail during the valuation report conversation. Mr. Blake asked about Observation Mix B, which decreases the expected rate of return but also decreases volatility and risk, which makes more sense to him if the goal is to increase stability and ensure that the funded ratio increases. Ms. Pizzi replied that this mix includes an increase to fixed-income of 35%, which seems high given inflation rate volatility. She said that if the BERS board is comfortable taking that level of return off the table, they can also consider Observation Mix B and a further increase in fixed-income asset allocation. Mr. Robins asked about assumptions of how many rate cuts the Federal Reserve will implement in 2024, and Ms. Pizzi replied that they try to base their assumptions on the markets' assumptions, which anticipate 3 cuts this year.

6.0 FY23 VALUATION REPORT – USI CONSULTING (FORMERLY H&H)

6.1 FY23 Valuation Report – USI Consulting (Formerly H&H)

Mr. Lemanski began by speaking about the purpose of the valuation exercise, which results in the valuation report for the portfolio each year. He said that the ultimate cost of a pension plan is based on the level of benefits promised by the plan, and that investment earnings serve to reduce the cost of the plan's benefits and expenses. He said that actuarial valuation seeks to assign a portion of the costs to the budget year, and is used to determine the level of the City's contributions to the plan. He noted that the Actuarially Determined Employer Contribution (ADEC) developed from the valuation has two components: amortization of unfunded liability, and normal cost.

Mr. Lemanski then provided an overview of the results of the actuarial valuation, comparing this year's numbers to last year's numbers. He said that the funded ratio declined from 69.7% to 66.9% since 2022, and compared this to the benchmark funded ratio for large municipal plans of 76.1% in FY22. He said that the preliminary ADEC for the City increased from $13.1 million to $14.9 million between FY23-24 and FY24-25. He said that assets performed well on a market basis (10.2%), and that asset smoothing showed a return of 5.4%, given that losses from previous years are being smoothed in as well. He said that this underperformance (smoothed asset return of 5.4% versus the assumption of 7.1%) drove the preliminary increased ADEC up by approximately $338,000. He spoke about the experience study and resulting assumption changes, which contributed to the preliminary ADEC increase of about $53,000. He spoke about other plan experience and its effects on the preliminary ADEC increase, noting that the largest driver was salary increases, followed by earlier retirements and fewer mortalities, many new entrants, and an expected increase in normal costs. He said that unfortunately, this all resulted in that significant preliminary ADEC increase.

Mr. Lemanski then spoke about assumptions and assumption changes. He noted that the BERS Board previously approved a scheduled reduction in the assumed rate of investment return from 7.5% to 7.0%, starting in 2019, but noted that the assumption remains at 7.1% for 2023. He noted that other large public sector pension funds had average assumptions of 6.91% (median 7.0%), and that the BERS assumption is in line with this. He noted that the mortality projection scale was not updated for 2023, given that the impacts of COVID may skew future projections for mortality, and the Society of Actuaries has paused on updating the scale.

Mr. Lemanski then spoke in more detail about the ADEC composition, showing a comparison of the 2022 valuation and the current (2023) valuation, as well as a comparison of the ADEC composition both before the experience study and after the experience study 30-year layered changes, as well as after 20-year layered changes. Mr. Kasti asked why the amortization of the unfunded liability after 20 years drives the ADEC lower for that timeframe. Mr. Lemanski noted that this plan since 2004 has been using a 30-year period for its layered amortization assumption, and that every year, a new layer is added as a rolling 30-year payoff. He said that in 2004, a 30-year amortization was common, but that since then, best practices have changed and that 30 years is too long. He said that they would like to propose two alternatives to the BERS board to the 30-year amortization, one of which is a 20-year "fresh start" beginning now, with subsequent changes amortized over 20 years, and a fresh start that retains 18-year (Class A) and 17-year (Class B) amortization, with subsequent changes amortized over 20 years. He said that the difference between the two options is whether the BERS Board would like to fresh start the current unfunded liability amortization at 20 years (or 17/18 years for existing amortization). He said that prospectively, these changes are the same, but that the 20-year fresh start has a short-term cost savings to the City's ADEC of about $720,000. Mr. Blake said that if they opt for the 20-year fresh start, the ADEC drops, but that any type of significant wage benefits that employees see will increase that unfunded liability at the rate that is not proportional to the increase in assets, based on the trends shown in the funded status slide. Mr. Lemanski replied that the funded ratio in 2017 (from that slide) is based on different mortality table assumptions and a different assumed rate of return, so the comparison across years is not necessarily apples-to-apples. He said that there has been an erosion in the funding ratio, but that the different assumptions makes it difficult to see a trended comparison based on current assumptions. Mr. Hooper noted that discussing this alternative would reduce the ADEC and cut the money going into the plan, and asks where the money not going into the plan comes from over the course of the 20 year period. Mr. Lemanski replied that the same benefits will be paid over time but it is a matter of timing of the funding, and that based on this analysis and if all assumptions hold true, the plan will attain 100% funded in 20 years. Mr. Kasti noted that the ADEC contribution is limited from year to year and it has a collar. Mr. Lemanski replied that they are not recommending future direct rate smoothing or a collar going forward. Mr. Blake asked whether the actuaries looked at an 18-year period for existing amortization, rather than bifurcating the Class A and B tiers into different schedules, and Mr. Lemanski replied that they did not look at this, but that it would likely result in an ADEC somewhere in between the two proposed scenarios. Mr. Blake wondered if bifurcating the Class A and B schedules opens up the plan for further bifurcation of these tiers in terms of other policies. Mr. Lemanski replied that there was no intent behind the bifurcation, but it was simply to show the effects of not changing the current period of amortization for each. He emphasized that they are not looking to continue with the 30-year approach, but would recommend moving to one of these 20-year scenarios.

Mr. Lessard then spoke in more detail about the funded status trends for the BERS pension. He, like Mr. Lemanski, noted that year-to-year trend comparisons between 2017 and 2023 are not apples-to-apples, given different assumptions around mortality and rates of return. He also spoke about comparing the funded ratio by using a market value approach versus an actuarial value approach, noting that the actuarial basis was much less volatile. He spoke about funded status by class, and the development of the unfunded accrued liability and funded ratio. He provided details about the summary of fund activity for the fiscal year, noting the breakdown and comparison between the market value analysis and the actuarial value analysis (with the former's approximate rate of return being 10.2% and the latter being 5.4%). Mr. Lemanski added that this is common for a mature municipal plan like the BERS plan, speaking about the negative cash flow that is occurring for the plan (which is normal). Mr. Blake asked for a historical analysis over the past 20 years of the impact on the pension of changes in contracts related to retirement for Class A and B employees, and Chief Administrative Officer Schad agreed that it would be valuable to look at those changes, but also to look at the changes in the assumptions and their impacts on the historical unfunded liability. Mr. Dow asked whether the City is in this situation because it has not followed best practices, and Mr. Lemanski replied that the City has remained aligned with best practice in terms of reviewing its experience studies and adjusting based on those.

Chief Administrative Officer Schad noted that the City's general fund is struggling this year with the reduction in federal funds and yet the City has a practice of fully funding the ADEC every year. She said that given this, she would like to explore the 20-year fresh start amortization, as that would also allow for a less steep increase in the ADEC and draw on cash between FY24 and FY25. Mr. Robins confirmed that this would be in line with best practice and with the approach that other municipal plans have taken. Mr. Kasti noted that it would also be equitable across employees.

MOTION by Katherine Schad, SECOND by Munir Kasti, to adopt the 20 years "fresh start" amortization policy for the current unfunded accrued liability, with subsequent changes amortized over a 20-year period.

VOTING: unanimous; motion carries.

7.0 ADJOURNMENT

7.1 Motion to Adjourn

The meeting adjourned at 12:04 PM.

RScty: AACoonradt