DRAFT

Burlington Retirement Committee

Meeting of the Committee Members

Agenda

April 8, 2014 5 – 7pm
Contois Auditorium, City Hall
149 Church Street, Burlington, Vermont 05401

Present: Mayor Weinberger, Bill Rasch, Joe Keenan, Councilor Bushor, Susan Leonard, Bob Rusten, Councilor Knodell, Councilor Paul, Eileen Blackwood, Mike Flora, Brian Lowe, Councilor Mason, Jim Strouse (by phone), and Joe Keenan (by phone)

Absent: Jeffrey Wimette and Bob Hooper (both expected to be absent)

5:00pm – 5:05 pm **Approve Agenda**

Approved unanimously

5:00pm – 5:05pm **Review and Approval of March 25, 2014 meeting minutes**

Approved unanimously

5:05pm – 5:10pm **Public Comment**

None

5:10pm – 5:50 pm **Discuss With Buck Consultants Their Ballpark Projections on Modifications to Actuarial Funding Method and Actuarial Assumptions**
David Driscoll via phone

David Driscoll: Asked by Bob Rusten whether changes in the actuarial assumptions would lead to substantial changes to the retirement system – of course, changes mean different things to different people.

- Impact of closure of amortization period: If the amortization of the System's unfunded liability were made subject to a deadline applicable to all year's additions or subtractions to the unfunded liability, each year's increment would be subject to more rapid amortization, and year to year changes in the City's required contribution would increase as a result.
- The projected unit cost credit method compared to the entry age normal funding method: David recommends replacing the projected unit credit method with entry age normal the practical advantage is that it is the method prescribed as the basis for financial reporting for public retirement systems under GASB 67 and 68. This method would establish a normal cost for each active participant in a retirement system as a level of percentage of pay that, if all assumptions hold, will remain constant
- Change the amortization method for the unfunded liability: Many public systems amortize unfunded liability in installments that rise with aggregate payroll, rather than in level installments. In Burlington, such a change (which makes more sense when combined with a entry-age normal funding method) would provide some financial budgetary relief at the expense of slower accumulation of assets and amortaization of the unfuneded liability.

- Impact of potential changes in actuarial assumptions: David argues that it is premature to change any of the underlying actuarial assumptions, with the exception of an expectation of greater longevity.
- Fixed rate technique: Another method David raised, this would identify a fixed contribution rate reset every *x* years and designed to capture the effect of benefit changes to new hires (since benefits generally are reduced for new hires since the earlier generation received benefits that have proven unsustainable)
- Blue Ribbon commission advocates "stress testing" of retirement systems (demographic changes, market downturns)

Councilor Knodell: David, with respect to the change in amortization method for the unfunded liability, you say our current arrangement it is more conservative, but not imprudent – is that accurate?

David Driscoll: The method you use now lays out 30 year plan every year for each increase in amortization (i.e., always 30 years from current valuation)…closure of the period would be similar to State of VT system, which has an amortization period ending on a particular date (2038). Were you to do that, you could amortize additions ("trailing pieces") separately, but each year you would have a more profound impact as the timeline shortens [and the period over which to pay for the increases lessens]

Councilor Knodell: What is the benefit, then?

David Driscoll: Ultimately, you would pay off the unfunded liability more quickly

Councilor Bushor: Could you explain how the changes in amortization schedule impact the unfunded liability? What do you mean by trailing pieces?

David Driscoll: Reviews City's current amortization plan, and how each year's new liability is added to the total and amortized on a constantly extending 30-year amortization plan.

Councilor Bushor: I understand that – it is like a mortgage where the principle is paid off over 30 years, but the increases are added each year and are carried forward on a new 30 year plan. Who pays for that? The taxpayer?

David Driscoll: The City pays for that.

Bob Rusten: Any questions? (none). David, can you speak to the closed vs. open system - Had we gone to the entry age method, the cost would have been about $300,000 more. The normal cost would remain more stable. (David - yes). If we had also gone to the level percent of pay, we would have saved about $1.4 million

David Driscoll: Yes, and that already includes the $300,000 difference you from the entry age method.

Bob Rusten: If we saved $1.4 million, but put in more than required to contribute and put half back in, $700,000 back in, what would the effect have been?

David Driscoll: You would have saved some money, and partly overcome the disadvantage

Eileen Blackwood: Is there a way of calculating how that would have affected the disadvantage?

David Driscoll: I could give you an amortization table showing the difference.

Bob Rusten: If we increased contribution amount, could it be modified to show that effect?

David D: Yes, I could show you that rather quickly.

Councilor Paul: If using a closed system approach, are we potentially overfunding the pension system?

David Driscoll: No – because we do evaluations every year. Were the system overfunded, usually you'd curtail contributions.

Councilor Paul: So that $700k could go to address the unfunded liability.

Mayor Weinberger: David, we are spending a little time later in the meeting talking about our investment strategy – and moving to a passive investment strategy with lower fees. How does your model take into account projected fees?

David Driscoll: I would work at others in Buck to make changes to the expected rate of return assumptions.

Mayor Weinberger: Currently, we are spending around ~$700,000 annually on fees. How is that accounted for in the model?

David Driscoll: It is in the model as against investment returns, so it could change the value held against returns – and we would of course have to change the investment model as well if you made changes to your investment allocation.

Mayor Weinberger: Are you familiar with the movement away from actively managed funds toward passively managed funds in the personal world? Have you seen this trend in the pension fund world as well? Our investment has underperformed the market, at least in the last 6 years.

David Driscoll: I have not seen that much [*in the pension fund world*]. People still think they can pick their manager or their investment fund effectively. People with defined contribution funds are more apt to do this – rather than paying the market to inflict damage on them. My sense is that because of your funds size, which would be an atypical allocation to my knowledge, but this is not my expertise.

Bob Rusten: Are there other changes we have not discussed that could make a substantial change?

David Driscoll: Maybe asset smoothing methods, but it would not likely make a lasting difference on your funding. Purely on the funding assumption and funding method side, there isn't a lot – maybe some relief. If the benefits don't change, the pattern by which you pay for them will not have much effect. Aggressive investment, that's another story – you could have higher returns, but there's also potentially greater volatility.

--- *no more questions for David, who ends call* ---

Jim Strouse: I'd like to follow up on David's point to say that I deal with investment funds across the country all the time, and it is actually very common to use the method the Mayor discussed as part of the investment strategy.

Bob Rusten: Jim, please hold that thought for a moment, as it's on the agenda later in the evening – lets deal with the actuarial assumptions first and then turn to that. Reactions from the group?

John Federico: I'd like to see the amortization tables so we can see the potential effect of the change side by side with the current system

Councilor Bushor: I did not understand the difference between and open and closed amortization system, and would want more information there.

Councilor Knodell: Clarification question – at the top of page 3 of David's paper (available on the Burlington Retirement Committee page of the City website), with the rolling amortization system, do you ever pay off the unfunded liability? And if you're an employee, wouldn't you want a date certain? It means the liability is paid off, and gives comfort that the City won't ever walk away, God forbid, from its commitments.

Bob Rusten: To clarify – the open vs. closed system is about an ongoing amortization as opposed to a date certain. The open or closed amortization is a particular methodology to use within that system.

Councilor Bushor: With the open system, my sense was that we would repay a substantial portion of the debt over 30 years, and would be left with a less substantial residual. Is that accurate?

Bob Rusten: How much we add to the unfunded liability each year makes a big difference as to what would happen over 30 years. Your question also gets to the discussion of what is our goal as a group – is it to reduce the unfunded liability, or decrease the City's contribution? Closing the system gets you a date certain – but it increases the City contribution.

Chip Mason: The benefit of reducing our liability up front is that it frees up dollars to work for us (the City's retirement system) in more productive ways.

Councilor Paul: I would also be curious to see the impact of shortening the amortization period. One of my goals is to eliminate the unfunded liability on a date certain.

Mayor Weinberger: It is not possible to say that in a defined benefit system. It is an uncertain, moving target. What we are talking about here could lead to paying down our debts more quickly, but it doesn't give us certainty of eliminating the liability completely.

Bob Rusten: I am hearing a different goal – system sustainability – in addition to reducing the unfunded liability.

Councilor Bushor: I agree with the Mayor – we can't assume we'll eliminate the unfunded liability when we can't know if we'll hit our investment return assumption, for example.

Bob Rusten: Would people like to see the impact of the closed system with the closed amortization?

(Yes)

John Federico: We should see as many as we can of these different combinations as we can to best address our issues. The Mayor is right that we can't have certainty, and we need to be fiscally responsible – the goal is to get as close to 100 percent as possible recognizing that we can't stay there.

Bob Rusten: We can do this, but it has a cost. David's work has cost $2000 so far.

John Federico: Using BERS funds to support the health of the system is an appropriate use of those funds.

Jim Strouse: I agree.

Eileen Blackwood: It may not be that expensive to get the tables John suggested. David made it seem like it's a couple minutes work in Excel. We should ask him for all of these things and see what the cost is,

Bob: We could also ask him for a model we can use ourselves.

Councilor Mason: Agree this is worth exploring.

Bob Rusten: So in summary, I will get back with David and bring back what we can to the committee to see the effect of making some of these changes.

John Federico: If part of this discussion is going to the BERS for cost, would you try to have that prior to the next meeting?

Bob Rusten: Yes – we intend to bring this to BERS at the next meeting. Now, we should turn to Mayor Weinberger's idea about a passive investment strategy.

Mayor Weinberger: Unlikely money managers beat the market on average over ten years, but the stock market has grown on average 10 percent a year (though there is volatility year to year). If the City can insulate itself from market volatility, it may be worthwhile to ask BERS to look into an index fund and see if we can capture the average market returns.

Jim Strouse: We asked our consultant (Barry Bryant) to do something like this – we should ask him to give us a recommended portfolio using these index funds. He is a little reluctant to do this, but I think he can, and I think this would be a good thing to do.

Councilor Knodell: Even with a passive investment approach, you still have to make some asset allocation decisions.

Mayor Weinberger: Yes – you have to have assets invested in a way that protects the next five years from market volatility, and you have to balance and update the remainder of the portfolio to reflect the market. But that is different than active management and substantially less expensive.

Councilor Bushor: Did David say this was unusual?

Jim Strouse: He was incorrect.

Councilor Bushor: I feel like we're moving from a bad position to an uncertain one. It doesn't give me warm fuzzies. There are risks here I don't feel like I fully understand.

Jim Strouse: I think the $100,000 figure (*in the Mayor's draft proposal for a fee estimate*) is too low – we would pay around $70,000 for a consultant and then we would pay another 1 or 2 basis points for a fee. That's going to be more than $100,000.

Councilor Mason: We may have some influence on VPIC's risk strategy (disagreement from Councilor Paul). But it sounds like they are moving to incorporate some of this into their investment strategy.

Councilor Knodell: Councilor Paul disagrees – I'd like to hear more.

Councilor Paul: We are a small component of VPIC and don't have influence over their decisions (Councilor Paul reviews VPIC's conservative investment strategy and the recent historical experience that led to that investment strategy). I would emphasize that there is no member of the VPIC Board who is there to represent the interests of Burlington.

Bob Rusten: To return to what we are talking about – do we want to take this proposal to BERS?

Mayor Weinberger: I'd like to look into more what other pension systems have done. I don't think this is a pioneering venture, but I am happy to do some additional research and make sure we are on solid footing.

Jim Strouse: I don't think you need to – send it to BERS and let us get to work.

Mayor Weinberger: Thanks Jim – let me do a little more work and we'll do that.

Jim Strouse: Sounds good, and talk to Barry. He deals with this all the time.

Bob Rusten: I suggest we look at Timeline and Workplan portion of the agenda next, as that will help us sort out thoughts on a consultant. We've reviewed the actuarial assumptions, investment allocation, and components of our system. Do we want to start looking at remodeling and different systems, which is something we talked about early on?

Mike Flora: I think it's time to start looking at the structure of the system – is a defined benefit structure sustainable over time? I've said this before – many other systems are going to hybrid models or direct contribution models for new employees. Is there some kind of sunset model we would look to – keeping the defined benefit system for current employees but changing potentially to a defined contribution system for new employees who are coming through the door so they know what they are getting up front. Ultimately it could help system sustainability.

Councilor Paul: Do you know of local municipalities doing this?

Mike Flora: Not local municipalities, but it is something happening across the country, and something I've seen when I research through Google or elsewhere.

John Federico: I don't think the committee should talk about remodeling – I think that's a question we should ask to a consultant.

Councilor Bushor: What is our retirement plan and do we need to modify it? It is a difficult conversation but I think it has to be part of the conversation. We can't just address the unfunded liability and not address the fact that we are continually creating new unfunded liability every year.

Joe Keenan: We don't know where we are on the curve relative to other municipalities, and that was something that came up when we started discussing our broader goals. We need to have answers about whether the system is broken before we start trying to remodel the system – maybe unnecessarily. That's where we need a consultant who can compare us to other municipalities – a key piece before we define our system as broken.

Jane Knodell: We know that since 2000 the total annual contribution has gone up substantially. Do we have projections out 10 or 15 years?

Bob Rusten: We can project that it will continue to increase, as the unfunded liability has continued to grow, but we cannot project whether the same exact trend will continue or whether it will continue at a different rate.

John Federico: The projections don't account for some of the changes that have already been made to benefits, based on David's comments about actuarial assumptions.

Councilor Bushor: I think we do need a consultant to assist here, even though there is substantive knowledge around the table.

Bob Rusten: Reviewing the areas we discussed previously, based on the discussion today, these are the five areas we've discussed exploring with a consultant with a new one added:

- Contributions to Fund
- Unfunded Liability
- Benefit Complexity
- Public Confidence in and Support for Pension System
- Recruit and Retain Staff
- Stability

Councilor Paul: There are people who can speak to changes in other municipalities (defined contribution, hybrid) and those outcomes, as well as to some investment changes.

John Federico: Someone like Hank Kim could speak to that, and draw on the resources of his organization (like NCPERS).

Bob Rusten: So I am hearing that (i) remodeling the system is about new employees, not current employees and that (ii) we as a Committee do need to look at bringing someone in who can look at different formulations of systems and speak to potential changes.

Councilor Knodell: John, do you know whether Hank Kim's organization's members have a variety of different plan types?

John Federico: I believe they have a handful of hybrid plans in their membership.

Bob Rusten: One other consultant we were considering was Keith Brainard. Brian, do you remember what organization he worked for?

Brian Lowe: He works for NASRA, the National Association of Retirement Administrators [it is actually the National Association of State Retirement Administrators], and I think his organization includes defined benefit and defined contribution members but I am not sure.

Councilor Knodell: I would note that the last group that looked at this concluded that a defined benefit plan was necessary to attract employees to the police department.

Bob Rusten: Considerations of remodeling the system does not mean defined contribution. I don't feel like I have good enough knowledge to make that judgment.

Mike Flora: I'd clarify that defined contribution for new employees is not necessarily something I'm in favor of, either, but it needs to be put out there.

Eileen: In reading up on this, it seems there are creative ways to make plans more effective and attractive, regardless of the different components.

Councilor Mason: We have day jobs – we need someone who eats, leaves, and breaths this and can speak to the range of possible options out there. We need someone from outside and then can debate the options that person can put forward.

Councilor Paul: We all have backgrounds that color our vision. An external actor can give us outside options without being shaped by a particular background.

Jim Strouse: Steve Harding of Gallagher Consultants could be an option – I'll look into it.

Bob Rusten: Can people agree that a consultant is someone that can speak to the system remodeling?

Councilor Bushor: If we are not changing our system, does it make sense to look at different options?

Bob Rusten: If we need to do due diligence, we should explore the full range regardless of what we ultimately decide to consider.

John Federico: Anything under the sun, for DB and elsewhere

Bob Rusten: So the focus of the consultant on system remodeling, broadly defined.

Joe Keenan: Can someone ask Hank define what "not as expensive" means?

Bob Rusten: We will get back to Hank, and arrange a short special meeting with Keith just to do the interview since he is not available at our normal time. And what about our timeline? We need to inform the Council.

John Federico: Lets limit the discussion to those two consultants.

Councilor Knodell: Since we don't yet have a consultant, unlikely to make the end of May. We should let the Council know and provide some kind of update.

Bob Rusten: The Councilors will arrange for an update with the Councilors, and we will arrange a special meeting and follow up on the actuarial tables, more from the Mayor on the investment strategy, and more from David Driscoll on the open / closed system.

Mayor Weinberger: How do we craft a scope of work with the consultant?

Councilor Knodell: We could do this in collaboration with the consultant.

Bob Rusten: Hank Kim noted that he could help us with the goals as well.

Public Forum:

Mr. Ruolff: The number 1800 is confusing – is that people collecting pensions or all employees. And if pensions underperforming by 6 percent, why not put money in U.S. Treasury for a guaranteed return?

Meeting ends at 7:04pm.

Next Meeting Time: **Tuesday, April 22, 2014 5pm – 7pm** (Location TBD)