TUCSON SUPPLEMENTAL RETIREMENT SYSTEM
BOARD OF TRUSTEES

Meeting Minutes – June 27, 2013
Finance Department Conference Room, 5th floor East
City Hall, 255 West Alameda
Tucson, Arizona 85701

Members Present:	Robert Fleming, Chairman Brandy Kadous, Elected Representative Lani Simmons, Human Resources Director Karen Tenace, Elected Representative Silvia Amparano, Designated for CFO John O'Hare, Elected Retiree Representative
Staff Present:	Michael Jesse, Lead Management Analyst Dave Deibel, Deputy City Attorney Melissa Waychoff, Administrative Assistant Michael Hermanson, Pension Administrator Michael Jesse, Lead Management Analyst
Guests:	Dana Woolfrey (Gabriel Roeder Smith & Co.) Cassie Langford (Yoder & Langford) via phone Doris Rentschler, Lead Management Analyst, PSPRS Staff Matthew Cline, AFSCME Mike Wisnieski, AFSCME Lionus Kafka, CMO Zoning Examiner Linda Hatfield, TACE Diana Amado, Mayor & Council Darren DaRanco, AZ Daily Star
Absent/Excused:	Allan Bentkowski, Treasury Finance Manager Kevin Larson, CM appointee Kelly Gottschalk, CFO and Assistant City Manager

A. Call to order – Chairman Fleming called the meeting to order at 8:31AM.

B. Consent Agenda
1. Approval of May 30th, 2013 Board Meeting Minutes
2. Approval of April 30th, 2013 Special Board Meeting Minutes
3. Approval of June 18th, 2013 Special Board Meeting Minutes
4. Retirement ratifications for the month of June 2013 – need changes to ratifications.
5. May 2013 TSRS expenses

Motion to approve consent agenda with date order corrections to retirement ratifications made by Brandy Kadous, 2nd by Karen Tenace, **motion approved 6-0 (Kevin Larson absent).**

C. Disability Retirement Application – Patricia Tolle* (reconsideration from March 2013 meeting)

Motion to approve Patricia Tolle disability application for purpose of discussing; made by John O'Hare, 2nd made by Brandy Kadous. **Brandy Kadous added a motion to enter Executive Session,** 2nd by Lani Simmons, motion passed 6-0. **Motion to exit Executive Session** made by Brandy Kadous, 2nd by John O'Hare, motion passed 6-0. On the **motion to approve** Patricia Tolle's disability application: the ayes passed with a vote of 6-0 (Kevin Larson absent).

D. Investment Activity Report Administrative Discussions
   1. Callan Associates – Paul Erlendson and Gordon Weightman
   2. BNY Mellon, New Fee Schedule and Contract effective 7/1/2013
   3. Portfolio composition, transactions and performance review

Agenda item 1 was carried forward to the August 29th meeting when Callan Associates will be here; items 2 and 3 were carried forward to the July 25th meeting.

E. Administrative Discussions
   1. Sustainable Retirement Benefits Act*

Linda Hatfield, local union President from TACE states they have been meeting daily regarding this issue. They met with the state Firefighters Association on Monday and are looking to hire an outside campaign organization that will probably cost $500K. They are in the process of garnering money from national resources and local sources to be able to pay for this campaign; they have developed a joint letter signed by three unions and are sending it to all of their members requesting they not sign the petitions and to educate family and friends of the issues involved; they are reaching out to all of their natural coalition partners as well as Veteran groups; they have scheduled meetings with the Mayor & Council; they are pulling papers to file a campaign committee which they have not named. They plan to hire a strategic consultant on July 18th and are reviewing strategic plans in other states to see what else has happened and how other jurisdictions have handled this issue. They are also putting together a video to be posted on YouTube and it will be done professionally. TACE has had a lot of people reaching out to them, which is excellent and they would also like to partner with CTRA.

Linda closed by saying the resolution is being written as we speak, but she wanted to know if there were any actuarial estimates available and what those were. Linda would like the resolution to state the adversity this would cause the City, and try to express the crisis that would occur. It is a resolution for the Pima County Democratic Party about how we do not want the City of Tucson to go bankrupt as a result of this. Linda Hatfield is waiting on numbers from the actuary for this resolution. Mike Hermanson stated that actuarial analysis indicates an increase to the contribution rate paid by the City of about 19% or $24M in the first year. Dave Deibel stated that, as a Board; we cannot take a position or give any advice on the matter. Lani Simmons stated it is very helpful and important for the Board to know what other activities are going on. Lani also indicated that Doris Rentschler is heading up the Pension Education Committee.

Mike Wisnieski from AFSCME stated they are handing out flyers every day, hitting the ground running.

John O'Hare asked if individual members of the Board can make comments if they preface that they are not speaking for the Board, just on their own effort and expressing their own opinion. Cassie Langford would prefer the Board just take this as an informational session. John O'Hare just wanted to be sure he could voice an opinion to people he knows. Cassie Langford stated it is important to be careful with those conversations.

Motion to enter Executive Session by Lani Simmons, no second, motion expires for lack of a second. Dave Deibel stated that he did not think the actuarial discussion needed to be discussed in executive session.

Dana Woolfrey, a consulting actuary from the Actuary firm Gabriel Roeder Smith & Company (GRS), will be presenting their firms estimates of how the TSRS plan will be affected, based on the proposal contained in the Act; also, Cassie Langford, TSRS outside counsel – both are attending via telephone.

Dana began the actuarial presentation by stating the City received an initiative filing called the "Sustainable Retirement Benefits Act", which makes it sound like they are saving the day; but, it is not a solution without tradeoffs. Frequently, when defined contribution and defined benefit plans are compared, the prevailing decision is to go back to the defined benefit plan.

If the DB plan were closed, there would be no new hire employee contributions, and because there are benefits that have already been promised to members already in the plan that have not been fully paid for at this time, the remaining burden to pay those benefits will shift to the City.

Traditional actuarial best practice would result in accelerated funding to closed plans. As a result of having a closed plan, the TSRS Board will want to consider funding policies that follow best actuarial practices. This could mean funding would have to be accelerated, increasing the Employer contribution rate quite a bit.

In a closed plan, if the City does not make additional higher contributions up front, the plan will end up being poorly funded over the long term. Projections indicate the plan will end up being funded at the 65% level in 25 years with the current funding policies; and if the Plan is closed and no change is made to the funding policy, it will fall to the 50% funded level with an expected downward trend. What's happening is that the employee contributions and employer normal costs are going into a defined contribution plan instead of to the defined benefit plan.

The amendment allows current members to opt into the new plan. We cannot predict who will opt into the new plan, but we looked at a "what if" scenario where all post-2006 hires opted out of the DB Plan. If that occurs, it will accelerate the underfunding of the defined benefit plan because it would be like closing the plan 7 years ago.

One of the questions being raised in discussions is - is it even legal for members to opt out?

The City's Bond rating is another issue because of the funding problem that would occur from the Act. With a reduced rating, the City's borrowing costs go up.

Under the new GASB Accounting, the City will have to report higher liabilities on their financial statements and closing the plan could make those numbers even higher.

With a closed plan, it will eventually have to be 100% funded because the last benefit payment has to get paid. The plan will need to accelerate contribution levels or its members, retirees and bond rating agencies will have concerns.

The only way a defined contribution plan can reduce costs for the City is to provide reduced benefits (there's no magic to this). Individuals do not tend to be great investors and cannot earn long term investment returns at the same level that the professional money managers in the pension plan can.
Also, in a defined benefit plan, if a member leaves, they do not get the City contribution back, but a defined contribution plan allows them to get the City contribution back if they leave. A DB Plan dollar is more geared toward paying retirement, rather than termination benefits.
The lack of a defined benefit plan can cause difficulty transitioning older workers out of the workforce and may cause difficulty with attracting and retaining employees in the workforce. As government pay has lagged private industry for higher pay and bonus compensation elements, without a pension benefit, the workforce will be looking for something to be added.

In a defined contribution plan, investment and mortality risk is shifted to the individual. In a defined benefit plan, the mortality risk can be effectively pooled among all the members in the plan.

Certainly, if there is one advantage from having a defined contribution plan, it's contribution rate stability, because there are no unfunded liabilities. Regardless of that, if the Act passes; the City will also need to make a decision on how to address the unfunded liability that already exists for the DB plan.

Defined contribution plans introduce additional work. Currently, the DB Plan has one trust that is professionally managed. With a Defined Contribution Plan, now you have 3,000 individual accounts that have to be managed – account balances that need to be updated daily, member statements that have to be mailed, member election changes...all that comes with a cost. It may be an implicit cost passed on to members in terms of administrative fees that lower there cost, but there is a cost.

Rationale for accelerating funding to the closed plan:

- Shorter time horizon (as no new members are coming in)
- Prefer to have plan funded by time last member retires, which would shorten amortization to 10 years instead of 20 years.
- A closed plan will force you to meet your funding commitments because you have to have the money available to write those checks. The only way a municipality could get out of paying promised benefits is if they went bankrupt.
- For an open plan, amortize as a level percent of growing payroll. Change to level dollar payments for closed plan

Liquidity is another issue; the investment strategy may have to change if more liquidity is needed to pay retirees with a change in the cash flow to the plan, and that could result in lower investment returns due to having to constantly pull money from investments.

For the Board's comparison, the actuarially recommended contribution rate for FY14 is 32.32% (City contributions plus member contributions), and that rate was adopted by Mayor and Council during the spring budget discussion; at the same time, the amortization period was changed from 15 to 20 years.

The Act indicates the City may amortize pension debt over total payroll, which is acting like the plan is still open and not closed, but would result in the defined benefit plan being more and more underfunded. The Act does not indicate what the employer match for the "401k-like plan" would be, so the City would have to address the amount they are planning to provide to the defined contribution plan. Without better information to indicate what the City match would be for the DC plan for new employees, GRS provided projections with 5%, 7%, and 9% contributions to the new DC plan. When looking at the scenarios assuming no change to the defined benefit plan funding policy, contribution rates under the 5% DC scenario are similar to those assuming the defined benefit is continued unchanged and slightly higher under the 7 and 9% scenarios. However, as previously stated, under all these defined contribution scenarios, the funded ratio is projected to drop from the 6/30/2012 level at 63.4% funded to a 50.1% funded level in the next 25 years and is still headed downward at that point.

These scenarios assumed the funding policy was not changed with the closing of the plan. However, best actuarial practice is to treat the plan as a closed plan, which requires that liabilities are amortized not over the current policy of 20 years, set by the average TSRS career period, but to change it to the average remaining future working years of active members; which, based on the TSRS demographics, it would be 10 years in the first year. In year two, it probably would not go down by a full year, it might change to 9.3 year amortization, perhaps 8.5 years in year three; so each year, redo the calculation. In a sense it is a closed amortization approach, but is based on actual remaining service life, so it might go not go down by a full year in any given year. Using the 10 year, level dollar amortization the current City funding rate of 27.1% would rise to 46.3% in the first year.

As the plan becomes better funded, the contribution rate starts to decrease. City contribution levels were high, but the plan is almost 100% funded 25 years out. Either the City overall contribution levels have to really increase or the contribution levels can stay the same and the defined benefit plan funding level gets worse over time. It does not make the unfunded liability go away when you switch to a defined contribution plan. As shown on slide 16 (middle column), projected funding requirements show that the City contribution level for the first year would increase from 27.09%, or $33.9M to 46.3%, or an increase to the City contribution of $24 million.

The Act allows current members to opt out of the plan. It would seem the post July 1, 2006 hires would be most likely to migrate because they have had the highest contribution rates relative to their benefits and would therefore have more money at stake in the plan. Slide 18 isolates the possible effect to the plan, should all members hired since July 1, 2006 migrate to the DC plan. It shows that in the case where contributions are accelerated, City contributions are increased from 46 to 49% of pay, and in cases where contributions are not accelerated, the projected funded ratio 25 years out moves from 50% to 38% funded.

Long-term, a defined contribution plan could meet budget objectives, but it does not address immediate problems. Mike Hermanson stated the Board will need to consider the TSRS funding policy again if the Act goes through and we would want to be prepared for this and ready to make recommendations.

Lani Simmons motioned the Board go into Executive Session to seek legal counsel regarding options to consider, 2nd by Karen Tenace, motion passed (5-1 John O'Hare opposed). Motion to exit Executive Session made by John O'Hare, 2nd by Brandy Kadous, motion passed 6-0.

Brandy Kadous asked what the Board's responsibility is as far as communicating to our members wanted to have a plan for that. Karen Tenace suggested other groups use their web sites and media to help employees understand their plans and benefits. Karen suggested it might be the time to do that to educate employees. Lani Simmons stated we are fielding inquiries and questions daily, but we are constrained as a Board to take a position. Doris Rentschler is preparing a briefing for Mayor& Council for July 9, 2013. Karen Tenace is concerned about the new GASB that will be very different than the numbers we received today and employees will see two sets of numbers and might be confused. It was challenging to educate people on the funding of TSRS during the spring this year, and this new topic will not be easy either. Doris will try to compile all the different pieces of information. The bullet point will be to educate the City that this act would cost the City $24M in the first year. Karen thinks there needs to be a simplified fact sheet and a more detailed sheet for people who want to see it. There needs to be a section on the TSRS web site for pension education. John O'Hare feels retirees should also be informed. This is moving fast and we are briefing people as quickly as possible. Silvia Amparano suggested the Board send out a letter just like the City Manager did. Karen Tenace thinks it should state what the Board's role is. Brandy Kadous suggested including a summary of the actuarial report.

F. Articles for Board Member Education / Discussion
   1. Public Vote Sought To Rein in City Pensions (*Arizona Daily Star* – June 6, 2013)
   2. Signature Effort (*Tucson Weekly* – June 11-13, 2013)
   3. Arizona Pensions not easily reined in (*Arizona Republic* – May 8, 2013)
   4. Creating a New Public Pension System (*The Laura and John Arnold Foundation)*
   5. City of Tucson Retirees Newsletter for June 2013

G. Future Agenda Items
   1. August Meeting: Callan Associates - Quarterly Review for June 30, 2013; Annual investment manager reviews for Champlain, Aberdeen and SteelRiver
   2. Reconstituting advisory committee in City Code (October meeting)
   3. Actuary's recommendations for improving the funded status of the Plan (October meeting)

H. Call to Audience – Lionus Kafka suggests a fact sheet should also go out to retirees.

I. Adjournment – **Chairman Fleming stated we are adjourned at 10:30AM.**

Approved:

7/31/13		07-31-13	
Robert Fleming Chairman of the Board	Date	Michael Hermanson Plan Administrator	Date