

CORAL GABLES RETIREMENT SYSTEM
 RETIREMENT BOARD WORKSHOP AGENDA
 WEDNESDAY, MARCH 16, 2016

8:00 A.M.

UNIVERSITY OF MIAMI NEWMAN ALUMNI CENTER
 6200 SAN AMARO DRIVE
 1ST FLOOR LIBRARY

MEMBERS:	A	M	J-11	J-25	A	S	O	N	J	F	M	APPOINTED BY:
	15	15	15	15	15	15	15	15	16	16	16	
Andy Gomez	P	P	P	P	P	P	E	E	P	P	P	Mayor Jim Cason
James Gueits	P	P	P	P	E	P	E	P	P	P	P	Vice Mayor C. Quesada
Charles Rigl	-	-	-	-	P	P	P	P	E	P	E	Commissioner Jeanette Slesnick
Michael Gold	P	P	P	P	E	P	P	P	P	P	P	Commissioner Patricia Keon
Rene Alvarez	E	P	E	E	P	P	P	P	E	P	P	Commissioner Vince Lago
Joshua Nunez	P	P	E	P	P	P	P	E	P	P	P	Police Representative
Randy Hoff	P	P	E	P	P	P	P	P	P	P	P	Member at Large
Donald R. Hill	P	P	P	P	P	E	E	P	P	P	P	General Employees
Troy Easley	P	P	P	P	P	P	P	P	P	E	P	Fire Representative
Diana Gomez	P	P	P	P	P	P	P	P	P	P	P	Finance Director
Elsa	P	P	P	P	P	P	E	P	P	P	P	Human Resources Director
Jaramillo-Velez												
Manuel A. Garcia-Linares	P	P	E	P	P	P	P	P	P	P	P	City Manager Appointee
Jacqueline Menendez	-	-	-	-	P	P	P	P	E	P	P	City Manager Appointee

Chairperson Hoff called the workshop to order at 8:07 am. All Retirement Board members were present and recognition was made that Mayor Cason, City Manager Cathy Swanson, Commissioner Keon, City Attorney Craig Leen, and Representative from the Fire Union were in attendance. City Actuary, Mike Tierney, was listening in by conference call. Dave West of The Bogdahn Group and Pete Strong and Jim Rizzo of Gabriel Roeder Smith guided the workshop.

1. Why it's good to have a funding policy?

Dave West explains that the purpose of the workshop is to provide a forum for constructive dialogue discussing the possible solution paths to take in order to minimize the unfunded liability and the strain on the City. He informs that the he is the investment consultant and this is largely an actuarial driven issue being discussed. He has had the pleasure of working with both Pete Strong and Jim Rizzo from Gabriel Roeder Smith through the Florida Public Pension Trustee's Association. There has been a huge push to come forward with some solutions for pension systems across the State of Florida to address these types of issues.

Pension liability can be broken down into two pieces. There is the normal cost and the accumulated cost or what is being called the mortgage payment on the unfunded liability. The normal cost is the cost of operations for any given year and the unfunded would be the liability generated by failing to meet the assumptions that were put forth as the funding approach to the pension system. If you look at the normal cost and changes to the pension participants are making larger contributions to the plan. There has also been a reduction in benefits that has brought down the normal cost. The big issue is the unfunded liability which began around 2000 when poor market returns began affecting pension systems around the country. Those systems had a higher rate of return assumption fell short by a wider margin than the plans that had lower rate of return assumption. There were system funding decisions made that began to accumulate the very large unfunded liability. These are issues that have been inherited by the current team. It is a legacy issue they are now attempting to address. Several steps have been taken already. Dr. Gomez asks what the unfunded liability amount is as of today. Mr. Strong responds that it is roughly \$240 million which is around 43% to 44% of the plan.

Mr. Strong continues with the presentation. The presentation stems from presentations given over the past year at the FPPTA Trustee schools. A Funding Policy is a written document that establishes the policies for determining how much and when should be contributed to a pension fund. It tries to accomplish a number of different objectives, some which are competing, but the ultimate goal is the long-term solvency of the pension plan and eventually reaching a 100 funded ratio. Developing a funding policy should be a collaborative effort between the City, the Retirement Board and the Union Representation so all interest can be reflected.

Most Boards already have in place an Investment Policy. An Investment Policy is a formal policy that that dictates fiduciary responsibilities, expected investment standards to follow, a criteria for monitoring and performance of assets, process for manager selection and defining what your asset allocation targets are. These guide the investments of the fund and for years there have been Investment Policies to help make those decisions. It guides future Board members. So a Funding Policy would be the same thing but on the funding side. The Funding Policy should including to describe the actuarial cost method, the asset smoothing method, the procedures to follow for evaluating and accepting actuarial assumptions, risk management guideline principals and general overall principals for funding the plan so that current and future Board members will know how decisions were made and what steps were followed to arrive at the Funding Policy guidelines.

Jim Rizzo states that Mr. Strong mentioned five elements of the Funding Policy. As part of the work with the FPPTA they have developed a sample template for a Funding Policy. They are not finished with it yet. There will also be an instruction manual which will provide great background and resources on how to create a functional Funding Policy. Those documents will be placed on the FPPTA website in the future. There has been a lot of momentum for Boards to actually adopt a written Funding Policy around the

Country. In 2013, The National Government Finance Association adopted a best practice to adopt a written funding policy. NASARA, the National Association of State Refinement Administrators, adopted a similar recommendation in 2013. NCPERS, the National Conference of Public Employees Retirement Systems, has a whole pension funding forum in 2015 where they talk about adopting a Funding Policy. The Society of Actuaries established a blue ribbon panel a couple of years ago in 2014. The Academy of Actuaries in 2014 adopted an issue brief. The biggest piece of the national organizations that are pressing this topic came from the Conference of Consulting Actuaries where numerous actuaries from around the Country from different firms had a Committee that developed a White Paper on funding policies for public plans. The Florida Statutes provide some guidance and outside limits but they are really incomplete for having a full useful policy. They just give outside limits.

Mr. Rizzo explains why a funding policy is needed. A Funding Policy helps Pension Plans gives structure and guidelines to the actuary rather than the actuary making decisions on their own. It shows all the interested parties that the Board has adopted a well-conceived and well-crafted Funding Policy. It's a public document. It helps fulfill promises to plan members. One of the most important responsibilities as Board members is to assure the plan is funded adequately and systematically on an actuarial basis. That is what the Funding Policy helps the Board do. The Funding Policy helps defend defined benefit plans against accusations. It helps prevent the State from stepping in and dictating how things should be done. It demonstrates compliance with State Statutes and actuarial and accounting standards. There are five primary elements of a Funding Policy: actuarial cost method, asset smoothing method, amortization procedures, actuarial assumption setting procedures and risk management process. You have to have a basis to make a decision so that is where your objectives are. There are five objectives that these national organizations have spelled out. They are fulfilling benefit promises to members with confidence, intergenerational equity, volatility control, accountability and transparency and separate the inputs from the results. The number one objective is benefit security as you set these five elements you are going to want to think thru which of their choices will enhance benefits security and which will not. These five objectives are competing with each other. The concept of intergenerational equity is basically you have employees rendering public service to the public and you have the public paying for it. Intergenerational equity says that there ought to be some reasonable connected between the public paying for these services to the people who are getting it. If you separate and have one generation of tax payers paying off an obligation that the City made to employees who retired a long time ago that is not equitable. Volatility Control is to avoid volatility in the employer contributions and in the unfunded liability. Accountability and Transparency is to maintain well documented policies and procedures so everyone reading it can understand what the policy is. The last is to avoid agency risk. Of the five elements there are five objectives to help you answer the elements. Economists like to use the term agency risk. You have employees rendering service in exchange for compensation paid right away and in exchange for compensation deferred for many years later. It is all that exchange between members rendering service and citizenry receiving

that service. The elected officials and City management serve as agents on behalf of the citizenry and Unions act on behalf of the members so that is the agency relationship. The Board is an agent on behalf of both parties to make sure the promise is fulfilled in a systematic way. What happens in agencies, sometimes, is that sometimes agents that are supposed to be serving these purposes have either their own personal interests interjected into their duties or some other interest that is contrary to their agency role. It is important to talk about making sure you avoid agency risk. He hears attorneys advising Boards around the State and if a Union member or a City member that serves on a pension board is able to take off their hat when coming into a board meeting because their fiduciary duty is to the operation of the pension plan and not to the Union or the City. Members need confidence and personal assurance that the pension fund will be there for a while. Benefit security is an objective that you balance against the other objectives to make sure that members can have assurance that the promise that was made by the City to provide them their pension benefit that they have worked for almost 40 years will take them through their retirement another 40 years. That is an important objective. Even the State Statute in Chapter 112.61 states that retirement plans are to be managed, administered, operated and funded in such a manner as to maximize the protection of employee retirement benefits. That is really a good expression of benefit security objective. Intergenerational equity is a concept that tries to avoid kicking the can down the road. Again, Statute Chapter 112.61 states that it should be fairly, orderly and equitably funded by the current tax payers as well as the future tax payers and to prohibit the use of any procedure, methodology or assumptions to transfer to future tax payers a portion of cost that may have been reasonably expected to be paid by the current tax payers. That is a general principal to go by. Volatility control has three elements that the funding sponsor is often concerned about. One is the volatility or predictability of the annual contribution requirement. The second is the volatility of the net pension liability. The third is the volatility of the funded ratio. Stability and predictability on these three metrics is a worthy method to try and work toward to balance the objectives. Accountability and transparency is to maintain well documented policy and procedures. Clarity in the description so there is no confusion. It is good to have clear and transparent policies to defend them. There is a lot of tension going on in the Country of attacking the management of defined pension plans so it is important to have a good, sound Funding Policies and one objective is clarity so that you can help defend what you have done. Consistency with best practices and recommendations of industry experts means that you don't want to be an outlier on what your policies and practices are. They talked at length about avoiding agency risk already. All of these five objectives help inform you when you go to judge what the five elements should be.

Craig Leen comments that the City of Coral Gables has taken a position in the COLA matter that Statute 112.61 about the transfer to future taxpayer a cost that should be paid by current taxpayers that it is enforceable. They have taken that position. It is a general standard but also an enforceable one.

Mr. Garcia-Linares asks Mr. Stone if he could briefly explain how the pension plan has gotten to the unfunded amount it is at today and also what was not done by prior administrations that aided in the unfunded amount. Mr. Strong explains that cannot be isolated to one thing. They had an array of different things happen. The number one cause was counting for roughly two-thirds of the unfunded liability was investment performance falling short of expectations from 1999 until 2014 even with the uptake they got in 2012 to 2014. The overall return they got for that period was about 4.5% over a fifteen year period. Back in 1999 and 2001 your expected rate of return was 9% so they came in about half of what was assumed and fifteen years of that you can see how you accumulated the liability. Roughly 30% of the funded ratio decline was due to investment experience. Mr. West believes in 2000 they had a 9% assumption rate. The pension fund is funded by a couple of different buckets which are the investments, member contributions and City contributions. So the investments fell short and that exacerbated the fact that there was less money from the investments going into the plan so it had to be made up somewhere else. Mr. Strong states that starting in the mid-2000 the assumed rate of return was first brought down to 8.25% then to 7.75%. Bringing that investment assumption return down from 9% to 7.75% increased the liability. That accounted for roughly about 9% of the funded ratio decline because of the changes. The other 7% to 8% were demographic assumptions. Mr. Garcia-Linares thinks that they have to work with the City to figure out how, over time, to pay off that unfunded. Going forward, if they don't hit their investment assumption this year, what should the City do to not continue an increase in the unfunded portion of the liability? Mr. Strong answers that assuming 7.75% is earned each year and we are smoothing any fluctuations. As of the last valuation date there was a cushion. They had three years of gains that are being smoothed in. He thinks for this year's valuation that the market value and actuarial value will be closer together. He thinks they will wipe out some of that cushion.

Chairperson Hoff states that when the City had the 9% assumption rate it was not out of the ordinary so there was the presumption that if we were on the same page as everyone else. That is the strongest point for considering having a Funding Policy because it takes into account that once all of the current Board members are no longer Board members their Funding Policy is a living, breathing document and that is why they are at this workshop today. Dr. Gomez adds that they have to create a Funding Policy that has flexibility. Mr. Strong adds that investment policies are often amended. Mr. Rizzo states that it probably should not be really easy to amend the Funding Policy without a compelling reason that is vetted with the Board as to how and why.

Commissioner Keon states that she has heard a statement before that the funding for the plan was not adequate in the past. Is there something that the previous administration should have done or did they not do something? (partially inaudible) Mr. Strong explains that the assumed rate of return on assets at the time were 9% on the year. The fund assumed that 9% on the investments was going to come in from investment earnings that year and at the time the contribution requirement was only a few million dollars because they were expected to fund the plan through mostly investment earnings. As they went

through 2001 and 2002 during that recession downturn and through 2008 and 2009, the average return turnover the last several years has only been less than 5%. That shortfall between what was expected and what was actually earned, the liabilities were growing at 9% a year but the assets were only growing at 4.5% to 5% on average so you accumulated the difference. Commissioner Keon understands that but doesn't understand what is meant when they say they took out a mortgage. Mr. Strong informs it is not really a mortgage. Mr. Rizzo explains that people use the term mortgage because that is a term people are familiar with. If you have a \$600,000 obligation that has to be paid off somehow and usually it is a leveled dollar amount for over a certain amount of years. When people call it a mortgage they are likening it to the obligation of the City. When some new liability appears it is because the investment return has fallen short and it creates a liability. Who do you think pays that liability? Commissioner Keon asks what action was taken by the City to address the liability issue. Mr. Rizzo responds that someone has to pay for the shortfall and it is the City. Every year is either a gain or loss and each one creates its own mortgage or obligation. Mr. Strong explains that each amount that is incurred each year is amortized separately so it is a layered obligation. If the amount isn't made on investment returns ultimately it relies on contributions coming in. Mr. Rizzo states that the liability will go up if that year there was a shortfall and that shortfall will get financed over 25 years. It may be that if the investments do better than assumed and will bring down the liability and then the contribution would come down for the same reason. Then you can maintain the layers of gains and losses and amortization payments that are spread out over the future. Ms. Gomez comments that the City has always made the required contribution every year. Mr. Rizzo states that if every year all the assumptions worked out as assumed to be then they won't be growing it will be coming down. Mr. Strong agrees. Over the last few years it has been coming down. Mr. Rizzo states that you need to make sure as part of your funding policy that you have a disciplined procedure for how to set the assumptions so you don't end up with overly optimistic assumptions or expectations that are outliers. If you did that you would have more losses than you have gains. That is why it is important to have the Funding Policy lay these things out.

2. Best practices

Mr. Strong explains the best practices of the primary components of the Funding Policy are. The actuarial cost method is influenced by all the competing objectives. It is how the normal cost is calculated and how benefits are allocated to years of service. The asset smoothing method is influenced by intergenerational equity, volatility control, accountability and transparency. The amortization procedures are influenced as well. The actuarial assumption procedures are influence by all five of the objectives and then the risk management process.

3. Funding Policy Components

The first component is the entry age normal cost method. Coral Gables Retirement System has been using the entry age normal cost method for many years going back to 2000. Entry Age Normal or EAN is the preferred method. It satisfies all of the competing objectives. It provides for intergenerational equity. It provides for volatility control as it targets a level percent of payroll funding throughout a persons' career. What Entry Age Normal does is it projects on an individual basis each members' projected retirement benefit assuming they have salary increases equal to what they are assumed to be and that they continue to work until retirement or the probability of leaving before retirement. There is an array of possible outcomes. It comes up with the total projected benefit and the liability of it. They allocate that over a person's career earnings. This is the preferred method. Most plans throughout the State of Florida use the Entry Age formula. It is the method required by GASB 67 and 68 accounting standards so he feels confident that the Entry Age Normal is where you want to stay and is where you are now. Having that information written into the Funding Policy would cement that.

The second component is the smoothing method. The Coral Gables Retirement System uses a five year asset smoothing method. What that means is any time the expected return differs from the actual return on assets the difference is spread out over five years. So if you were expected to earn \$25 million return during the year but your actual return was \$15 million you would have a \$10 million shortfall but you would only recognize \$2 million during the current year and \$2 million each for the next four years. It smooths out those fluctuations over a five year period. Each year you have another piece that compares what actually happened versus what was expected. It is to help smooth out volatility. It doesn't do that much to harm intergenerational equity but they still recognize what happened during that five year period which you can say is in the same generation. It does a good job satisfying the objectives. The five year smoothing method is the most common method used to smooth out volatility. It is the maximum allowed under Florida Statutes. Some States use a higher than five year smoothing period. They also have an 80% to 120% maximum corridor around the market value. So if they have several years of bad experience in a row or several years of good experience in a row such that the difference of the smoothed actuarial value and the market value exceeds 20% it is capped at the 80 to 100 corridor around the market value so the smoothed value won't deviate too much from what your market value of assets is.

The third component is the amortization period. The maximum amortization under the Florida Statutes is 30 years. Last year the Board made a decision to reduce any new amortization basis to be amortized over 25 years instead of 30 years. The 30 year amortization period is considered by experts to be too long. It has been the subject of a lot of discussion by national organizations. It spreads across into the next generation. Mr. Rizzo adds that originally the 30 year amortization was set by GASB as an outside limit. It wasn't a recommendation to actually use 30 years, it was an outside boundary. But everyone used the 30 year amortization. Just because 30 years is allowed does not make it appropriate and a lot of people in the industry now think it is probably too long to

amortize things because you are spreading out the payment of the obligation out over into future generations.

Ms. Gomez asks if the minimum required contribution is based on 30 years. Mr. Strong explains that the minimum required is based on the Funding Policy. Mr. Rizzo comments that if the Board decides that 25 years is the right period for amortizing then that is the required contribution the City has to make. Mr. Strong states that the GFOA has said that the ideal amortization period is between 15 to 20 years to balance volatility control within intergenerational equity. They are current at 25 years for all amortization bases and some have fewer than that because they have been in existence for longer than five years. Most of them have fewer than 25 years remaining. Mr. Garcia-Linares asks when they set up the Funding Policy can they put in the policy that says going forward that new amortization will be somewhere between 15 and 20 years. Mr. Rizzo informs that the instruction research manual for this has a section on transitioning. You can transition from current policies and there are mechanisms from transitioning into the new policy. Ms. Gomez states that the shorter amortization period for the losses would make it more expensive on annual bases for the City to contribute. Mr. Rizzo agrees but if their assumptions are good it will be offsetting.

Mr. Easley asks for Mr. Strong to clarify the costs of going from a 30 year to a 25 year amortization. Mr. Strong informs that they made that change last year and it was only a few hundred thousand dollars difference. Mr. Garcia-Linares asks for a recommendation as to the number of years they should have for amortization going forward. Mr. Strong thinks it makes sense to have different amortization periods depending on how the unfunded liability was created. If an unfunded liability was created as a result of a plan change or assumption changes that may be a different amortization period than a liability if it is from an experience gain or loss. That is something for the working group that comes up with a draft Funding Policy to work through.

Chairperson Hoff states that he is hoping that at the end of this workshop that the Board can decide to proceed on creating a Funding Policy. He thinks the best method to do that would be to have the Investment Committee meet, come up with the Funding Policy and make a presentation back to the full Board. That way they can have City representation on the Investment Committee. He thinks that is what they are looking for once they are done with the presentation.

Mr. Strong continues. The Conference of Consulting Actuaries White Paper states what they consider best practices amortization period is to be within the 20 to 25 year range for assumption changes bases because you are recognizing all at once any potential future gains and losses that are happening over time. For actual gains and losses they are recommending 20 years. Commissioner Quesada asks what the financial impact is from moving the amortization from 30 years to 25 years. Mr. Strong responds that 30 years is the maximum amount of years under the Florida Statute. That has been in place for many years. Going to 25 years last year had an impact \$122,000 on the City contribution

requirement. Switching from 30 years to 25 years didn't really change the payment but it saved on the interest. Mr. Rizzo adds that if they were amortization bases that were created in the last five years there were some gain bases and some of them were shortened. Commissioner Quesada asks what the rationale was of the CCA to change from 30 years to 25 years. Mr. Rizzo explains that the few actuaries who liked 30 year amortization thought that a longer amortization period for assumption changes to make the assumption changes less expensive. That is the one or two on the committee who liked 30 years but the overwhelming majority thought that even for assumption changes it should be shorter than 30 year amortization.

Commissioner Keon asks of which assumptions were changed. Mr. Strong explains that they did a comprehensive Experience Study was done and changes were made to retirement rates, determination or turnover rates, recommended salary increase rates, which actually created a cost decrease to the disability occurrence rates, and the mortality rates because there was a requirement by the Florida Legislature to require pension plans to use the FRS Mortality rates. They did touch on the investment return assumption but they did not make any changes to it. Mr. Hoff states that the Experience Study was done to assist in the decision making of the Board. Experience studies are performed once every 5 years to review salary increases, turnover, retirement rates, etc. The last study was completed in December 2014. Mr. Rizzo explains that much of what they are talking about will become the topic of the work during the meetings to set up the Funding Policy. Ms. Gomez asks if the State of Florida requires that an Experience Study be done every five years. Mr. Strong informs that it is not required, it is recommended.

Mr. Hill asks about the rate of return assumption. Mr. West has told the Board in the past that he doesn't expect the stock market to make 7.75% every year that it is expected to be lower. Is that correct? Mr. West responds that they are putting together expectations for the probabilities of the asset allocation to achieve the rate of return and they go about it a couple of ways. One of the ways is to use capital market assumptions. In their forward looking capital market assumption they did slightly lower the expected return for equities but they lowered the expected return for investment grade bonds investments. When they put the forward looking capital market assumptions together for the asset allocation and run the modeling that results in a slightly lower return expectation. The second way they did was backward looking experience going back many years they were able to achieve a higher return historically than what they were expecting going forward. Mr. Hill asks if they are overly optimistic by expecting 7.75% a year. Chairperson Hoff comments that they are not going to go down that road. These are issues that they will address down the line once they create this funding policy. Mr. Strong states that based on the recommendations for the funding policy it doesn't state what the assumptions are but it lays out the ground rules of how to set the assumptions. It sets the policy to look at the assumptions rather than to set the assumptions.

Mr. Strong continues. Mortality rates now set by law. They are the same as FRS. They usually update the mortality rates every five years. It was last updated in 2014. It is not

due to be updated until 2019. The risk management process is the fifth and final component for the funding policy. Setting the risk management process it's multi-dimensional. You need to consider the risk tolerance of the plan sponsor who is making the contribution each year. How much tolerance do they have in terms of if adverse experience was incurred and it called for the contribution to increase? What is their threshold of risk? Knowing the threshold risk can help you to set parameters to control that risk. Enterprise risk management goes beyond what your risk metrics are. It goes on to what effect deviations have on the sponsor itself. There is a feedback for an enterprise risk management process. First you look at the risk management of the sponsor and how much risk can they accept. That effect of the risk profile of the portfolio of assets of the plan. Then based on that risk profile you set the actuarial return assumption and do some asset liability modeling and see the risk appetite. It becomes a feedback loop. Doing asset liability modeling shows what would happen if they were to go through another 2008/2009 down turn. These are scenario tests that should be done to gage risks and see what would happen. Mr. Rizzo states that if they always do projections of future contributions based on the assumptions that are all satisfied and they never are it is important to know what the downsides are before making decisions like benefit changes, asset allocations, etc. Risk management often is focused on portfolio. Enterprise risk looks at the bigger picture. It looks at the effect of the risk profile of the pension fund and the effect on the City, on the contribution, on the unfunded liability or on the funded ratio and that helps guide the Board. There is this balance. The less volatility you want on the annual required contribution means that your returns are going to be lower. You have to find the equilibrium that the Board and the plan sponsor can come to an agreement with. That is what enterprise risk management is about. Mr. Strong informs that he has already sent the Board samples of funding policies.

City Manager Swanson-Rivenbark states that some of the changes that may be anticipated that the City can't plan and so they would encourage as they are looking at this funding policy how can they make sure that the transition of the changes they may be proposing are absorbable by the City for a reasonable period of time. Mr. Rizzo replies that they will work with the work group to give examples on what the impact is. Chairperson Hoff comments that from the very beginning the first presentation he sat through regarding the funding policy without a doubt is a partnership between the City, the administration and the Board and the recipients of the fund. There has never been any intention to force the City to do anything other than what they have to as fiduciaries to this fund. The Finance Director/Trustee has done an admirable job from the beginning advocating for the City and making sure the Board considers all aspects of the fund. There has never been any intent to try to force the City to do anything. When the funding policy comes out the investment committee is an excellent committee because it has representation from the appointed Board members, it has representation from the elected Board members and it has representation from the City. He thinks it is a well-balanced mechanism they have to institute this. Their responsibility and duty on as a Board is to the fund whether they are an employee of the City or an appointed member. The reason he is saying that the Investment Committee is the best to do this because it is the best

representative of the whole Board. It is a standing committee that doesn't require any additional responsibilities. As Board members they have a fiduciary duty to the fund as required by the City Code and the Florida Statutes. There has always been an attempt to try to balance between the needs of the City and as an individual Board member believes what is best for the fund. Mr. Easley states that the recommendation through the Experience Study the actuary indicated to the Board to look at adopting a mortality table that was more aggressive than what the State was coming out with and they decided to hold off from adopting that. The State recommended a less conservative mortality table than the one they were going to go with and they decided to step back from that and hold off and wait.

City Attorney, Craig Leen, thinks they made a mistake when they say they have a fiduciary obligation, which they do, but it can't be oversimplified. The obligation is a balance and you have to make a functional system that works. Mr. Garcia-Linares comments that their obligation is to the system. Mr. Leen states that in his view you can't put a personal obligation above an obligation to the fund. When you are talking about fiduciary duty that comes up when you hold self-interest above the fund. He thinks that these are general issues and there is a balance and it is appropriate for the City to raise their interest or a union member to raise their interest. Mr. Rizzo states that they should look forward and look at the other cities that are 100% funded and how did they get there and what have they done to get there. What are the other sources of income those cities used to fund their system? Mr. Strong gives an example of one of his clients that is 100% funded. Every time their funded ratio went down they made extra payments to try to catch back up. From the 2008/2009 downturn they went as low as an 80% funded ratio they made extra payments to get caught up. The extra payments plus the market swing up helped them get back to 100%. Mr. Garcia-Linares states that if extra payments were made to the fund in the past and the investments were doing well they would not be here. They have to separate this into two. They have to figure out what happened in the past and then going forward let's not continue to increase the unfunded because they need to fund additional amounts.

Mike Chickillo of the IAFF states that he has been coming to the Retirement Board meetings for a few years and a couple of years ago the Board recommended changing the mortality table and they were asked to hold off due to City finances. Pat Salerno was instrumental in that and a lot of the payments were delayed. Chairperson Hoff comments that there were assumptions that were made and there were assumptions that were not changed. They went half-way. Those are issues that the Investment Committee and ultimately this Board will address in the future. This workshop is solely for the purpose of understanding a funding policy and determining whether or not they want to move forward and how they are going to do it.

Mr. Garcia-Linares thinks this is a two-step process. First is creating a general funding policy saying going forward they will fund the plan. Mr. Strong agrees. Their recommendation is to establish a work group to come up with the parameters of a funding

policy. Mr. Garcia-Linares states that step two would be implementing that plan which could mean looking at assumptions and other things going forward. Mr. Strong doesn't know if it would result in immediate changes. Mr. Garcia-Linares suggests that if the City wants other members of the City to also partake in this work group they should work on it together. Mr. Leen doesn't think the Retirement Board can set a funding policy for the City. The City is paying extra payments to the fund and it is a sovereign policy of the City. He thinks it is a funding policy in terms of the plan's assumptions and that the City would be part of that because they have a funding policy affected by that. Mr. Garcia-Linares asks if they could recommend to the City a funding policy and that it is up to the City Commission to adopt the funding policy. Mr. Strong explains that the five components of the funding policy can be set by the Board. They already are being set by the Board. They are just not in one place in a formal document. Mr. Hoff states that this is coming together so they all can work together. He understands they can't make policy for the City but if City staff is involved with the development of the policy and the Commissioners and Mayor want to push it along then it becomes policy for the City also. Mr. Leen thinks that they can't forget there is an agenda item that was deferred pending this meeting which was to review two actions of the Board. Mr. Garcia-Linares asks what actions he is referring to. Mr. Leen responds that it is the mortality table and the investment assumption return. Commissioner Quesada agrees with Mr. Garcia-Linares that if the funding policy was put forward by this Board it is only a recommendation that the Commission would review. Mayor Cason thinks they all need to understand that the City wants to have a very healthy retirement system which is why they are making additional payments to the plan. Mr. Rizzo comments that the State Statute charges the pension board with operating the plan and administering the plan including determining the required contribution. Mr. Leen explains that Coral Gables has a deemed-to-comply pension plan under State Law and under the City's Code the Commission has the ability to review for cause actions of the pension board. Commissioner Quesada states that at the next meeting the Board can make a motion that will be clear of the intent and will not be in conflict with Mr. Leen's thoughts.

Chairperson Hoff asks what the two issues are that Mr. Leen has referred to. Commissioner Quesada explains the way he understands it the mortality rate is set by law but the implementation does not have to go into effect until next calendar year and it has an impact of about \$900,000. However, this Board has approved to implement the mortality table for this year which would have an impact of \$975,000 but they are not required to implement it until next year. His perspective with these facts tells him is why implement it this year and pay the \$975,000 when they don't have to start until next year. What is the benefit of implementing it this year? Mr. Strong answers that when they did the Experience Study and the \$975,000 increase would not only apply this year but for the next 25 years as they pay off the liability associated with the mortality table. Because it is a total increase of \$12 million to \$14 million that is amortized over a 25 year period, he believed and recommended to the Board that it would be better to pay it off sooner rather than later. People are living longer, the Experience Study showed that, and they recommended a more conservative mortality table than the FRS mortality table. When

the legislation passed for pensions plans in Florida to begin using the FRS mortality table and since it had a late effective date and they had tabled the decision previously to go to a more conservative table, he recommended to go ahead with the new mortality table because the mortality table had not been changed for a couple of years and people are living longer based on their Experience Study. If you started paying for it now it's one less year you have to pay for at the end and you are starting to fund the true cost of the effective future benefits. It seemed to be the more prudent thing to do to start recognizing that change. Mr. Rizzo adds that the Society of Actuaries publishes mortality tables based on the most recent data collected on the universe. In 2014, they adopted a new mortality table and published it. The previous one had been done in 2000. The 2014 table showed that people everywhere are living longer. FRS's own Florida experience showed people are living longer so he thinks that was the basis of the recommendation at the time pending the State Statute. Ms. Gomez remembers that the experience of mortality was not so different than the actual mortality of the retirement system. Mr. Strong informs that the one thing they were recommending that was significantly different from the current assumption was while it is true that current experience was not much different than what actually was assumed, mortality has showed to be improving each year. Because of the improvement each year, incrementally, the table that is in place now is astatic mortality table and not expected to incorporate future improvement in the life expectancy. The expected life expectancy is five years longer than it was 20 years ago.

Mr. Gold comments that they are talking about a lot of major issues. First of all they are talking about a \$240 million deficit and 100% is probably aspirational. They are also talking about mortality tables and mortality reality really changing. The investment returns are changing. The investment assumptions and actuarial assumptions of the plan they may or may not actually acquire. They are looking at that all in context. When they look at those three or four things and see the whole they are trying to dig themselves out of and make sure they are doing the right things to work towards, that \$975,000 didn't seem like a lot and it was a compromise at the Board level at the time. They take it all in perspective and they aren't trying to stick it to the City. They are trying to do the right thing for everyone and make sure they can all get along and hold it together.

Commissioner Quesada states that they have a difference of opinion in strategy. He wants to do everything he can to pay down as much as possible now. The way he sees the \$975,000 is that it is being taken away to pay the mortality assumption. He thinks to himself if he had a \$100,000 mortgage and he was able to pay down an additional \$15,000 today so his payment will be less in the future. The lower they can get the unfunded liability now the easier it will be to be the most conservative, most proactive, most forward thinking City out there. He wants to chop down the debt as much as possible before they are thinking 25 years down the road. That is his perspective. Mr. Strong understands. He points out that as of 10/1/2016, if you want and adopt the mortality table at 10/1/2016 instead of 10/1/2015 the liability on 10/1/2016 is going to be exactly the same on 10/1/2016 if you adopt the mortality table now. Mr. Garcia-Linares

thinks the issue is how much of a dent is paying the \$975,000 do versus going ahead and changing the mortality table. Mayor Cason adds that they can use that money to pay down certain other amortization bases. Mr. Garcia-Linares thinks that it is the issue. How much is paying that extra \$975,000 would do versus changing the mortality table. Mr. Strong explains that it just changes the required contribution amount for the fiscal year. It is either you are going to make the changes 10/1/2015 or 10/1/2016 and once you are at 10/1/2016 the liability is going to be the same as if you waited. The total unfunded liability is the same. Ms. Swanson believes that this is very relevant and the City Commission is interested in taking action and this feedback with the Board is very helpful. They are not trying to reduce their payment; they are trying to bring down the unfunded liability of the plan. That \$975,000 can go to paying off some of the debt. They understand the mortality table has to be changed for 10/1/2016 but they can use that \$975,000 to put it toward the accelerated payments the Commission has opted to embrace.

Chairperson Hoff comments that he truly appreciates the exchange of information and it is very rare that the Board and the City meet to discuss these issues. His perspective is whether it is the investment consultant, the actuary or the attorney, the Board receives recommendations from any one person in that particular field. When their actuary came before the Board and gave a recommendation. They all want out from under that liability. The Board agrees with you. When he first started on this Board someone explained to him that a pension is a very simple thing to calculate. It costs whatever amount it takes to pay the last participant and how the plan sponsor gets is really a bunch of guesses they are going to make somewhere along the line. So having that basic understanding of the pension plan and knowing the fact that as citizens everyone wants to get out of that unfunded liability. By waiting an additional year to implement the tables that should have been implemented since 2008 because the system was using tables from the early 1980s. They went from the 1980s to 2000 projected and they took the steps they believed based upon the actuary's recommendation and because that becomes an unfunded liability they are actually helping more. That is his mentality and his presentation of the pension plan and why they did what they did. Ms. Gomez thinks sometimes there are conflicting objectives. The actuary wants to be conservative and have conservative estimates for the Board to agree to. The higher objective for the City now is to pay down the unfunded liability and not do anything else. Mayor Cason asks if the Board was given the a choice to either pay the mortality table early or take the \$975,000 so the City can see if that amount could be better used to help the Retirement System by paying down some of the amortization bases. Mr. Strong informs that at the time of the recommendation he and the Board were not aware of extra payments being made by the City. They recommended going forward with the best assumptions. If he had known, he would have given the Board a choice and shown them the options. Mr. Garcia-Linares asks how much of a difference it would make to pay down the \$975,000 now of the unfunded and wait a year to change it versus doing it now. Mr. Strong answers that they are one year closer to fully funding the plan starting now versus a year later.

Mr. Garcia-Linares states that the way he looks at it is that for a \$240 million unfunded they are arguing over \$1 million. It is either they pay an addition \$1 million now or next year so you are putting off the \$975,000. Percentage wise they are talking a minimal amount. Commissioner Quesada asks what would be more conservative about paying off your debt. That is what they are trying to get. They will have more money to give to the employees and more money to give better benefits to the employees when everything is fully funded and protected. Every dollar they can get to pay down the debt makes sense. Mr. Garcia-Linares asks what the cost of the second issue is. Mr. Gold states that the issue is more of an accounting issue and not a dollar issue. He thinks the City is concerned about how this is accounted for because all the dollars are going to the same place. Ms. Gomez states that the additional payment to the unfunded makes the funded ratio go up and the unfunded liability go down which for the City is what they want to show. Mr. Strong informs that it will be the same regardless. You have a total of \$26 million coming in and that is the payment towards the unfunded in the aggregate so the funded ratio and the unfunded liability will be the same regardless. Mr. Gold states that taking the line of the most aggressive assumptions is what got them to this point. It is one of the major details of one of the five major things to look at to come up with a funding policy that they think the City will buy into and they want to work together but they want to get off the edge and that was part of getting off the edge. They can kick the can down the road and be as aggressive as they want to be on everything and have less principal commitment but it also does not work like a mortgage. That is an easy way to oversimplify it. It is a mortgage if your mortgage accrued every year and created new liabilities every year and you were assuming you had to grow at 7.75% every year so they have to work with those variables too.

Chairperson Hoff asks what the second Board action was that the Commission is going to review. Mr. Leen responds that it was the investment return assumption. Mr. Garcia-Linares asks what change the Board made to the investment return assumption. Ms. Gomez responds that the Board did not make a change. The Board reflected that the City come back with acceptable changes to the investment return assumption. The actuary had recommended that the Board move to 7% over the next three years. The Board asked her as the Finance Director that the City come up with an acceptable plan for the investment return assumption rate. She presented the recommendation of staff to the Commission of what they can do. Dr. Gomez was there and he asked that the Commission defer their action until this workshop. Mr. Garcia-Linares understands from the Board's actuary that the first thing they should do is put this funding policy together. They don't get to that issue until they work on the funding policy. They are not changing the rate. They need to work on the funding policy and then work with the City to see how they can implement it. Chairperson Hoff thinks that perhaps there was some confusion because there was not a point that he anticipates in the near future of changing the assumption rate. They had a workshop in November. The purpose of that workshop was to accomplish what he hopes they have been able to accomplish at this meeting. The investment consultant and actuary during their presentation in November brought the issue up of the investment assumption rate and that became the major issue. Since he has

been on the Board the investment assumption rate has been a major issue. They have had many discussions about the investment assumption rate but if they are implementing the funding policy they have many steps to go before they change any of the assumptions other than the legally required mortality table. He does not anticipate that it is an issue in the very near future unless it is required by the State like the mortality table change is. Perhaps the question to the Finance Director may have been confusing as to where they were going with this but in his mind changing the assumption rate is something that is not coming down the road any time soon.

Mr. Rizzo states that one of the elements of the funding policy is how to go about setting the return assumption. This work group can recommend to the Board anything they want to. Their recommendation to the work group is to set up a disciplined framework for learning what the experts are forecasting for future returns and the setting of the discount rate is not a lever to balance the budget. It is the Board's best expectation for what future returns will be. Whether it increases contributions or not is not part of the funding policy but the framework that the funding policy will allow some latitude. He thinks the direction they are going now is a really important process of how to set the return assumption. It is not set on if you can afford it or not, you set it based on the expectation of what the portfolio will bring and then you value the obligations accordingly.

Mayor Cason asks what percentage of cities use a funding policy. Mr. Strong responds that this is a relatively new movement. The FPPTA the last year just started educating trustees about this. They are having a lot of similar discussions with their other clients. They have actually only implement a few funding policies. Mr. Rizzo adds that outside of Florida, larger state-wide systems have funding policies.

Ms. Swanson-Rivenbark informs that she was at that workshop in November where the investment assumption rate was discussed. The response from the Board in the recommendations were very clear for the Finance Director to come up with a plan to lower the investment return assumption rate. The City will have to absorb the changes. The decision of using the FRS mortality is still on the table and according to Chapter 50-93 of the Code allows for the Commission to reverse the decision of the Board and that issue will come back to the Commission for further discussion. Mayor Cason explains that their concern was that they want a very healthy retirement system and without any discussion they have put in additional payments to the plan. When they read the Retirement Board minutes about the Board implementing the mortality table sooner than what is required by the State of Florida is where the concern came from. Chairperson Hoff doesn't think it is undoing what the Commission has been doing. It is applying it differently. Their goal is also reducing the unfunded liability. They are not trying to be counterproductive. They want to work together. If they have a retirement related question or any issue that appears before the Commission they will be happy to make their experts available to the City in addition to them being available to the Board. Commissioner Quesada asks if they can provide a simple explanation as to how not paying \$975,000 now or next year is the same. If they pay now as opposed to next year

he still doesn't understand how it is the same. Mr. Garcia-Linares asks for the actuaries to put something in writing explaining how this is the same. Mr. Strong states that if you were to table the FRS table until 2016 and you do the accounting on the extra \$975,000 that will come in and apply the extra payment toward an amortization base with only a few years remaining instead of one that has 25 years remaining you would reduce the required payment associated with that \$975,000 more quickly than applying the \$975,000 toward the 25 year base. Mr. Rizzo thinks they have covered a lot of material but there is one topic that has not come up. He is not concerned whether something starts this year or next year but when they do this year's valuation they have a hard time using an out of date mortality table in even measuring. If you talk about cutting down a tree, maybe the tree is higher than you think it is because people are living longer so that is why they recommended a more up to date current mortality table. They one they are using now is out of date. That is part of the concern they had as the actuary is that they perform the current valuation with an out of date mortality table. Don't under estimate the issue of using an out of date mortality table in favor of a budget consideration. It doesn't make much difference. Mr. Strong points out that they are bound by the Actuarial Standards of Practice and he has to qualify the report and it could be an issue if they believe that the current mortality table was significantly out of date. Commissioner Keon states that it is important to the City to reduce the unfunded liability for so many reasons. If not changing the table for this year is a wash they can reallocate those dollars to the unfunded liability or they increase the contribution because the mortality table change. It doesn't seem to make a difference because it doesn't affect the stability of the plan but it is a great benefit to the City that they pay down the unfunded liability for those reasons. If it is a wash it doesn't make any difference. That is what they are asking for today. Mr. Rizzo states that it is commendable to contribute more than the funding policy. He wishes all their clients and their plan sponsors had that mentality. Mayor Cason thinks this has been a great discussion and that they need a funding policy. He is glad they are going to hold off on any changes until they get their policy.

Mr. Garcia-Linares comments that he has been on this Board for a very long time and they have never had anything like they have had today. It has been very helpful and he would like to find out how they can do this again. Instead of it feeling like they are fighting each other let's get in a room and try to work things out. He appreciates all of them for coming. The next time there is an issue either come to the Board meeting or ask one of the Board members to come to the Commission meeting but they should discuss it as opposed to what sometimes feels is a pull from both sides. This has been very helpful.

Workshop adjourned at 10:31 a.m.

Kimberly V. Groome
Administrative Manager

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