PUBLIC RETIREMENT SYSTEMS' ACTUARIAL COMMITTEE

Tuesday, June 7, 2016
8:00 a.m.
House Committee Room 2
State Capitol
Baton Rouge, Louisiana

MINUTES

1. Call to Order

The meeting was called to order by Chairman Daryl Purpera at 8:05 a.m.

2. Roll Call

Members Present:	Mr. Daryl Purpera, Chairman, Louisiana Legislative Auditor (LLA) Ms. Barbara Goodson, Vice Chairman, Designee for Commissioner Jay Dardenne Senator Barrow Peacock, Designee for Senate President John Alario Representative Kevin Pearson, Designee for House Speaker Taylor F. Barras Mr. Jim Napper, Designee for Treasurer John Kennedy Mr. Gary Curran, FCA, MAAA, ASA, EA Mr. Charles Hall, FCA, MAAA, ASA, EA
Also Present:	Mr. Rick McGimsey, Proxy for Ms. Goodson at beginning of meeting Senator Beth Mizell Ms. Shelley R. Johnson, ASA, MAAA, Actuary, Foster & Foster Actuaries and Consultant Mr. Paul Richmond, MAAA, ASA, EA, Manager of Actuarial Services, LLA Ms. Liz Martin, Secretary

3. Election of Officers

Chairman Purpera nominated Senator Peacock as chairman of the Public Retirement Systems' Actuarial Committee (Committee). Mr. Henson seconded the nomination which passed with no objection.

Mr. Purpera nominated Representative Pearson as vice chairman, and Mr. Henson seconded the nomination which was unanimously approved by the Committee.

4. Approval of Minutes – January 21, 2016, Meeting

Representative Pearson moved to approve the minutes of the January 21, 2016, meeting. Mr. Henson seconded the motion, and with no objection, the motion was approved.

5. Discussion of Actuarial Assumptions for Louisiana State Employees' Retirement System (LASERS) and Teachers' Retirement System of Louisiana (TRSL)

Mr. Hall said that the Committee asked LASERS and TRSL to consider lowering their discount rates. Both systems hired an independent actuarial consultant, Mr. John Garrett with Cavanaugh Consulting, LLA to perform an independent review of their current situation and impact of lowering the discount rate. Mr. Hall introduced Mr. Garrett to the Committee and stated his qualifications, certifications and experience.

Mr. Garrett said he was given the task of reviewing LASERS and TRSL's current actuarial valuations and also reviewed LLA's valuations on the systems. Using a power point presentation, Mr. Garrett explained his research, review and results using current guidance in the Actuarial Standards of Practice (ASOP). The LLA's actuary used a different set of capital market assumptions. The retirement system board has hired and put their trust into an investment consultant who consults with them on the allocation of those assets. That information is very specific to how those allocations are set and if they use a different set of assumptions, may have come up with a different allocation of the assets in the first place. In order to be more consistent, he believes that they should use the investment consultant's capital market assumptions that were used in determining the allocation of the assets. They used the same information in defining what the reasonable ranges were for investment rate of return for that portfolio. If we use other assumptions, we would have to say why we are going to use this specific allocation of the board when we had a different set of assumptions. The board using those assumptions might come up with a different allocation in the first place. There is a little bit of a disconnect that we think could introduce some variability of result.

The other thing is that the systems' actuary, Foster & Foster, prefer to use longer term set of assumptions and the LLA actuary used a shorter term outlook. Discussing the duration and favoring the shorter term of assumptions… the longer term is what we think is the correct set by the Conference of Consulting Actuaries (CCA).

Senator Peacock asked him to define what he meant by time frame – long term versus short term.

Mr. Garrett responded that short term is typically 7-10 year time frame, and longer term is 20-30 year time frame. He prefers 50 years, but unfortunately 30 years is as long as he has seen. It is becoming more prevalent for investment consultants to provide longer term assumptions but years ago all they could get was 7-10 year short term output but now it is more common to provide longer term expectation. We favor the longer term that the CCA and their report talks about when developing funding valuations that we should be looking at long term expectation of investment rate of return because it is more stable.

Further findings were that when reviewing the LLA's sustainability report, we see that there is a lot of good news in that and when compare historical and current funding ratios both TRSL and LASERS have increased at a faster rate than what we see in typical plans around the country. We surveyed about 126 large plans of which these systems are a part of that. We do agree that there is a trend in the discount rate to further lower it. Under the same survey of 126 large plans what used to be in the median years ago was 8% and also the most common assumption used for public plans has moved down to 7.75% and pretty soon will move below that. If you did the survey today, the median expected rate of return would be 7.55%.

The trend in reducing the capital market assumptions from the investment consultants as well as the assumptions set by the large public plans is certainly a clear trend in lowering. We do believe that a funding policy that looks at this frequently may be more often than five years and considers looking gradually reducing that rate of return assumption is going along with the trend of large plans. That is one of the three aspects that actuaries look at when setting a discount rate: what does the data say; the investment consultants, capital market assumptions, statistical analysis, reasonable range, mid-point of the range; and where we are at for providing a discount rate assumption. It is equally important to look at how other similar plans are situated. A general sense of where the plan has been and where is going as well. To give a little more detail, looking at the setting the discount rate, we take the capital market assumptions and this is a sample close to the standard deviation of what is expected with Louisiana plans but we take that and come up with the information provided to give a range of expectation. The ASOP says they were written prior to the current set we have and this changed in 2013. Required reasonable range for this assumption to be wide enough so that it is equally likely that the return will be within the range as it is outside the range. So between the 25th and 75th percentile, in the middle of the distribution, was a reasonable range in the definition of the ASOP.

We construct still even today, even though not specifically written in the ASOP, it's not prohibited in the ASOP, we still provide that same type of analysis to see how wide that reasonable range is. So the larger the volatility of the plan then the larger this range is going to be. You can see going out 50 years, the range of reasonableness for an investment rate of return assumption for a system that has a standard deviation of around 15% is from 9 ½ - 6 3/4, so this would be the initial set of what the reasonable range would look like – a very wide range.

Mr. Garrett continued explaining that the typical process would be to focus in at the median of what those returns are. The median return for this distribution is very long point 50 years and beyond sometimes is the same as the geometric mean. So we focus on that and why it is important again, if it is a fund valuation we want the stable contribution results, calculation of the required contribution to be as stable as possible therefore the expectation is that over time the gains and losses will be offset. So we have a 50% likelihood of a gain as well as 50% likelihood of a loss. Those gains and losses over time were expected to offset meaning that the contribution rate calculated in valuation using midpoint assumption would be the most stable.

Talking about what's wrong with a little conservative bias and yet we see that if looked at both processes, we agree with both. It's just using the information is different than what was used for the capital market assumption and therefore for the allocation of the board. If we take the result of that which was earning a 7.4% discount rate and compare it back to the process that we would typically follow, we would say that that would be a little lower than the mid-point of the expectation and being lower means that it has a greater likelihood of producing a gain. A gain bias is called a conservative assumption. A lot of people tout that they would prefer to have conservative assumption. It's an issue with actuaries and we hate to deliver bad news and prefer to deliver good news and that gains have occurred instead of bad news. But again we are focusing on a valuation for determining a contribution rate over a long period of time. The importance is that we should not be biased and not expecting more gains than losses or main losses than gains.

Mr. Purpera asked when he says using a different consultant that puts us below the median. Is that simply because of assumptions that are different or because the other professionals have a different guess?

Mr. Garrett responded that the capital market assumptions that were used by Mr. Richmond included the capital market assumptions of the systems' consultants as well, but he just had 6-7 other firms in there so it did produce a different set of assumptions to then determine what the midpoint of those ranges – the reasonable range and the midpoint of expectation would be. I think if I remember, 7.4% was actually on the high side of his range of reasonableness.

Mr. Purpera said 7.4% was the discount rate. Mr. Garrett said that Mr. Richmond's midpoint of reasonable range was about 7.15-7.2%, and based on his assumptions, he has a loss bias.

Mr. Purpera asked if they averaged eight consultants in a highly complicated methodology, when he comes up with a number just below the median point of what the one consultant would be, then are you now saying that makes it conservative?

Mr. Garrett said yes, slightly conservative bias, 35 basis points different. Mr. Purpera asked if it is conservative only compared to that one market consultant. Mr. Garrett said based on the capital market assumptions that the professionals serving the board versus the seven or eight. One other thing too is the timing of it, so capital market assumptions move through time so not talking about the same exact set of data.

Mr. Purpera said he understood, but Mr. Richmond took an average of all eight consultants. You are saying that the average comes out a little less than what the board selected consultant say, so therefore you are saying that that makes it conservative. Mr. Garrett said the preferred process is that the allocation is very specific to those boards and based on one set of capital market assumptions from their investment professionals. A very specific allocation was used which might have been different had we used those other sets of assumptions. Mr. Purpera said he agrees with him but questions if they should be considering the results of eight consultants as a barometer to look at and not to say that Mr. Richmond is wrong.

Mr. Garrett said both were reasonable assumptions that followed the base and both were fine but we would prefer to use the board's capital market assumptions that were set to use the allocation.

Mr. Purpera asked if he agreed that looking at the other seven has some value and said that it sounds like a reverse argument because to use only one consultant seems to be biased especially if one is higher than the others. Mr. Garrett said it could be biased on either side – high or low, but the other side is why to use one specific allocation, because the board could have an infinite number of allocations if we could use some of the other capital market assumptions of some of the other professionals the board might have come up with a different decision on how to allocate the assets – put more or less into bonds, or stocks.

Senator Peacock asked for an explanation of point four on page 8 of Mr. Garrett's presentation, "Conservative assumptions result in greater likelihood of future gains and therefore, a trend in decreasing contribution rates." He asked how much more conservative could you be to say that a lower discount rate is going to decrease your contributions. Mr. Garrett said when we want to pick a mid-point – that median expectation of return – if we pick something that has a greater expectation of a gain, so the median is the 50 percentile. If we pick an assumption that is only 75% likely that the actuarial return is going to be below it, so we are very gain biased, we'd be moving to like a 6% - 6 1/2% return. So we are more likely to have a gain, the expectation is that it is more than 50% likely that the actual experience of the plan will have a gain more than a loss. So if we are expecting more gains in the future, those gains are then going to decrease the initial calculation of what the valuation contribution rate would be. So when we use that 6% rate of return, and have a great expectation to have gains, the cost of that would be the liabilities would be much higher because using a much lower discount rate. If you have a much higher contribution rate required up front but that contribution rate would not be stable because again we are expecting a greater likelihood of gains than losses so over time that very high contribution rate would come down and eventually in an infinite view get to the point and time that whatever the 50 percentile was, if that was truly what experience was, it would match up but take a very long time for that to occur.

Senator Peacock asked if he was saying that over time your rates will be a whole lot lower. Mr. Garrett answered yes, much higher up front with a more conservative assumption that decreased over time because you are expecting more gains than losses. Gains reduce the UAL and therefore reduce the required contribution. What we are talking about in reality though is the difference between the 7.75% rate of return and a 7.4% rate of return expectation and discount rates. So it is very minor. The difference is about 3% in the expected rate of return. So if 7.75% is the midpoint, then 7.4% would be the 53rd percentile, meaning that only 47% likely that the return would be less than that. So it's very tight and very close, but to infer that one is reasonable and one is not doesn't make sense because they are so close and both well within the reasonable ranges as we determined.

Representative Pearson asked if the systems could find an advisor with a more aggressive asset allocation and if they increased their asset allocation more aggressively. Hamilton Liner, NPC might come out with a higher assumption and we should be using something such as that.

Mr. Garrett said the process on how this is set typically is the investment consultants provide to the actuary their capital market assumptions. The system would provide what the target allocation is so those combined and the actuary would then determine the reasonable range. Although the investment consultants might determine with their geometric mean is or their arithmetic means are for that portfolio, the actuary really does a little more in depth and sometimes even models 5,000 stochastic runs from a distribution. The process then is the allocation was set by the board based on the specific consulting and the information provided by the investment professional. Sometimes that is modified and sometimes added to by the investment staff of the board but typically that process is done periodically as an asset allocation study. An asset allocation study is not done every month or every year but typically every couple of years. This policy should not be volatile but want to set it and see what kind of results you are getting and then revisit it.

Representative Pearson asked how Mr. Garrett advises other pension systems with higher assumptions or lower assumptions with similar asset allocation mix or does he say 8.25% is fine because they are more aggressive. Mr. Garrett said based on his experience most of the investment consultants determine their capital market assumptions every year and set for all clients as one set of assumptions used for all their clients. Now some clients may come up with a different allocation target based on what their goals are but it is one set of assumptions used for all the clients of that investment consultant. For example, Callen would set their capital market assumptions for 2016 and find it on their website, same as for Wilshire and NEPC will all have one set of capital market assumption. They can say the geometric mean, the arithmetic mean, and the standard deviation of that asset class and how it is correlated with all the other asset classes. That is really what we are looking for with capital market assumptions.

Mr. Purpera asked if the investment rate of return was 7.75%. Mr. Garrett responded the investment rate of return versus the discount rate. Mr. Purpera said the rates are 7.75% versus 7.4%, comparing Mr. Richmond's rate with Foster & Foster. He asked if that is actually the investment rate of return. Mr. Garrett responded that is the discount rate and that both used identical reductions from the investment rate of return assumption to get to their rates. So the difference in the discount rates are 35 basis points, and the difference in the expected rate of return was 35 basis points.

Mr. Purpera asked when talking about investment rate of return if it is really 7.75% plus 35 basis points. Mr. Garrett agreed and explained that 8.1% is one and 8.15% for the other is the investment rate of return assumption because one has a lower administrative expense offset.

Mr. Purpera said the same is true of Mr. Richmond's viewpoint is a cushion that you have to add to it. He asked Mr. Garrett to address if reasonable by looking at the rest of the nation. NASRA's information on 126-127 public systems shows a chart with 7.5%, 7.25% and there is a distribution shown in their report. When we get to the numbers above 8%, there is only maybe five systems out of the 127 that have any numbers above 8% which means we are in those five right now.

Mr. Garrett said he knows that NASRA does a great job of compiling information and would hope that when it says investment rate of return that it is only the investment rate of return. Now the systems could have answered the survey with the discount rate but still thinks it is reliable.

Mr. Purpera said he understands the investment rate of return and discount rate can be different for certain reasons and that is allowed by ASOP. We know some of those reasons, but probably out of 127 systems 100 use the same number. Mr. Garrett agreed. Mr. Purpera said about 100 of the systems are between 7% and 7.75%, most of the systems' assumed rate of return is going to run around the 7.75% today. Mr. Garrett agreed and said that is specific to their portfolio and target allocation. Mr. Purpera pointed out that Mr. Garrett's presentation confirms exactly what his actuary has been saying for a while that we need to move it down and know the systems agreed with that. Today most everyone else is 25 basis points below us. We are talking about gradually going down over five years. Mr. Garrett said timing matters too because not everyone is on the same cycle of developing their investment rate of return assumptions. The capital market has changed dramatically from 2007 versus 2009.

Mr. Purpera said if we stay at the current rate – hopefully not – but let's just say the Aon Hewitt of the world say at best in the next 10 years will have about a 6.5 – 6.9% market. If our systems stay at 8.15% or 8.1% or 8.05% then we will pile up some losses. Mr. Garrett said the key is for a valuation to determine a contribution rate, and long term that contribution rate will be in effect for 20 something years and to be stable we use the midpoint assumptions. Mr. Purpera said he agrees and his concern is that if we don't adjust the rate quickly and get to where we need to be then in the next 10 years, there is a likelihood that we will add more net investment losses and I think this Committee will be under pressure to do something more drastic with these systems.

Mr. Garrett said the market returns goes through a smoothing process so it does not go straight into the UAL and the effective funding. Because of the volatility of markets that is something that everyone should desire to have that ability to have some experience offset and some time to actually get to alternative experience to offset before you have to effect the funding. So asset smoothing is a very good feature that buffers the effect of market volatility on the contribution rates and it spreads the cost over a fairly long period of time in funding.

Mr. Garrett continued his presentation saying that the key is if we set a contribution rate that is used on any other sets of assumptions, again we want to be midpoint. If you want to determine how much would it cost to fund the plans fully in 17 years that is a different valuation with a different horizon and perhaps a different set of assumptions, but definitely a different set of methodology to get to that number. The key is the simple calculation that produces a funding valuation number to be used in budgets for a long period of time then we want that to be set at midpoint.

We do not see that the assumptions are materially different – 7.75% versus 7.4% - even if you add the pieces back on, both would have the same investment rate of return assumption. But if we just trop that – we looked historically at what a portfolio that has the standard deviation of return around 15% is what we saw on the capital market assumptions for both systems. We looked at how volatile this is. This is just one scenario of possible future returns and not much difference than what experienced in the past but we see 50% segregation results and a lot of volatility in market returns in future years. If we chart those two different discount rates – 7.75% versus 7.4% - they are right on top of each other, so it is hard to say if one is a reasonable earning and the other is not. The volatility of a typical public plan today, and saying that one is 35 basis is not within the reachable range, is difficult.

Mr. Garrett said the 2015 valuations showed some good news is being experienced because payoffs of UAL are moving faster than originally predicted. There was also a sustainability report given based on a stochastic model of the systems. We saw it produced the 75% likelihood that the plans would be fully funded by 2044 and in my experience that is pretty remarkable and thought it would reason for horn blowing and party hats. When we typically get 75% would often result in a plan lingering around and toward 0% funding and a plan not sustainable.

He further reviewed the historical funded ratios of both systems. The graph on page 12 of his presentation shows LASERS compared to the aggregate public plan survey by summing all the liabilities and assets of 126 plans surveyed. TRSL's plan was likewise compared to the aggregate public plan on page 13. Over the same period time of 2010 to 2015, the aggregate public plan surveyed was fairly flat whereas LASERS and TRSL's plans have improved in their funded ratios. Mr. Johnson also calculated how much the funded ratio would have improved had the plan maintained the higher discount rate it had years ago because the discount rate was dropped by 50 basis points during this time period. Also the systems changed from projected credit normal cost methodology to an entry age normal cost methodology. Both systems also had about a 4.7 – 5.0% reduction in the funded ratio during that period of time. Not to say that the other plans in this aggregate would have also changed their discount rate over this period of time but certainly it has changed the funded ratio of the Louisiana plans.

This shows that the work that has been done of changing the discount in 2012, the Act 399 legislation that passed regarding COLAs is having an impact. The statistic that he has seen is almost a billion dollars of UAL has been paid off that was not anticipated. We would think that you would be a little more congratulatory on this process. I have a lot of systems that would love to have had experienced a 6% improvement in their funded ratio over the last five years to be honest with you. Certainly the trend in discount rates is moving lower. The median plan discount rate of 7.75% is dropping to 7.5%. We see no advantage in being ahead of trend, and the reason is that the trends change and so if you get too far ahead of the trend because it will reverse at some point, then you are further behind than you want.

Mr. Garrett said we do agree with the recent legislative act that would remove the administrative expense from being netted out in the investment return to actually have it in a direct funding method so a contribution rate based, we agree with that. We find fewer and fewer plans are netting the administrative expenses out of the investment return and the reason is that the administrative expenses fit a pattern of growth more closely related to payroll than it would be through the investment rate of returns. So it's a better fit and more stable result in adding to the normal cost or simply a direct add-on contribution rate for funding administrative expenses. Of course, it is also in better alignment with GASB 67/68 as they require that the investment rate of return is not net after the administrative expenses are removed from the assets.

When we consider lowering of the discount rate, there are a lot of difficulties with that. The measurement of the liability goes up dramatically even with even a minor adjustment in the discount rate. A lot of plans struggle with that as they lower the discount rates and we have seen Calpers when they moved from 7.75% to 7.5% and spread it out over a couple of years. We are working with plans today that are also lowering their discount rates in Connecticut and phasing into it. Spreading out the impact is the method preferred for funding.

In summary, based on our review of the information provided, we do find that Foster & Foster did develop reasonable rates of return, and a reasonable range, and the discount rate assumptions do comply with the actuarial standards of practice. The same with Mr. Richmond's work and agree it is reasonable and in compliance with ASOPs. We prefer that again using the same set of capital market assumptions used by the board in determining the allocation of the assets is more consistent and provide more consistent results over time. If we use any other shorter term or other consultants' assumptions we could be introducing a source of instability. The effect of recent legislation and the changes in assumptions are making improvements and do see that the funded status here is again improving faster than any of my clients and any other typical plans out there. Again we see a continued trend of a decrease in the discount rate from 8% to 7.5%.

Senator Peacock asked about the phase in plan over a 3-5 year period from 7.75% to 7.5%, or an alternate plan.

Mr. Garrett said two different ways to change the discount rate. Over five years, the systems would probably want to do a step rate by changing the assumption in each valuation. To select an alternate approach, the valuation would be performed today would use a pattern of discount rates that already show a pattern of decreasing from 7.75% to 7.5%. So the valuation liabilities would be built on those assumptions already being in place whereas step rate by pieces. This valuation all future discounts are down at 7.75% and the next one all future discounts are at 7.7%, and the next one continually .05% lower. It is typically not effective to use the selective alternate approach when phasing over a short period of time.

Mr. Purpera asked from page 14 of the presentation that states, "No advantage for being ahead of trend", but he read in a report that the average investment return assumption around the nation of a public plan is 7.62%, and our investment return assumption is 8.14% - which is a big gap. Mr. Garrett said it is roughly half a percent. Mr. Purpera said he agrees in declining but to get ahead of the trend would take extremely drastic measures, so that statement is a little misleading. Mr. Garrett said when talking about the average allocation of plans and not specifically what Louisiana's allocations are, because Louisiana does have a little bit higher allocation toward stocks than the average plan. The average plan has about 52% allocation to equities, whereas Louisiana is a little higher. The capital market assumptions of the other plans have a reasonable range using the capital market assumption and allocation that the midpoint is around 7.75% nowadays and moving toward 7.5%.

Mr. Purpera said if we use the average of the eight largest which these two systems are part of, and then slide it down into the average using a very complicated method then it is more conservative. To have $3.4B in net losses right now shows that they have not been earning in the past.

Mr. Garrett said if they went back and did an experience for either of the plans based on the eight different consultants we would have had a lower number at that point in time but that is not the process that should be used. He asked why use the actual allocation of the board but not the actual capital market assumptions that were used to determine that allocation. Mr. Purpera clarified that he did not question that process but believes we need some evaluator of whether or not they are right and cannot just take on face value.

Mr. Garrett said the trend is established as a large group of large public sector clients and now you are one or two of those 126 plans at the top of the investment rate of return assumption. Each of those developed theirs based on predominately the capital market assumptions of their investment professionals and their allocation, so because you produce a higher expected rate of return you will probably always be higher than the trend. All we are saying is that the trend is showing that it is declining.

Mr. Purpera pointed out Mr. Garrett's comment that "because we produced a higher expected rate of return", but clarified a higher target. Mr. Garrett said there are other systems that use an NEPC that are in that survey as well, and other systems use Aon Hewitt. Because their target allocation may be different they would produce a different result.

Mr. Purpera made the point that to get ahead of the trend would really take some movement and that is not what we are contemplating and Mr. Richmond's proposal was just to catch up. Mr. Garrett said if you do expect the future returns will be 6% then if arguing between 7% and 7.5% and 7.4%, we are both going to produce very large increases to the UAL if that's the case. The difference between these as far as the return expectations and what we are actually going to get is going to be pretty minor. Mr. Purpera said so we are not arguing 7.75% and 6.9%, we are arguing 8.1% and 6.9%. The 6.9% was Aon Hewitt's numbers on the internet.

Senator Peacock asked if on page 13 Mr. Garrett is advising to move 25 basis points over the next five years at .05% each year. Mr. Garrett said that is one process to phase into the lower discount rate over five years and the systems' actuary has produced what the impact of that will be.

Senator Peacock expressed appreciation for Mr. Garrett's presentation and said they would contact him if any further questions.

Senator Peacock and the committee approved skipping to agenda item #7.

7. Discussion and approval of September 30, 2015, annual actuarial valuation and the required contributions and dedication of revenues contained therein for the Louisiana Assessors' Retirement Fund

Mr. Curran presented a summary of the Assessor's Retirement Fund valuation, pointing out the essential numbers and changes in the report. The large balance in the funding deposit account can be used to reduce future contributions or pay future COLAs. The balance actually exceeds the $12M UAL of the plan so without consideration of that balance, the funded ratio is 88.15% in terms of the impact that balance would have. It is in the market value of assets in calculating the actuarial, but for funding purposes it has been excluded. The board has decided to defer on paying off the UAL right now, because regardless the UAL will be paid off in four years. The employer's normal cost dropped from $11.4M to $11.1M and the amortization cost is up only because it was scheduled to go up and not a reflection of gains and losses because the UAL is frozen. At the end of the day when calculating the required contributions they have dropped from 6.75% down to 4.75% so the minimum recommended contribution is sitting at 4.75%.

Mr. Curran commented that this report shows the change in the valuation interest rate to 7% net of investment expenses. Since the plan is smaller and in an effort to reduce risk the rate has been reduced the last couple of years. The funding of the plan also includes ad valorem revenue sharing which is a significant component of the funding. The boards elected to leave the contribution rate at the 13.5% level for the last couple of years to build up the funding deposit account balance as a reserve for contingencies and to pay COLAs.

Mr. Curran offered a motion to adopt the report and the assumptions therein and accept the minimum recommended employer contribution rate for 2017 to be set at 4.75% and that the funds shall receive the maximum allocated amount of ad valorem taxes and revenue sharing provided for by law for fiscal 2017. The motion was seconded by Senator Peacock and with no objection the motion was approved.

8. Discussion and approval of a technical amendment to the Municipal Employees' Retirement System of Louisiana's June 30, 2015, valuation report

Mr. Curran said after the valuation was completed, they concluded that the projections for mortality tables which had been scheduled to use scale AA were used accordingly but the female projection improvement rates were not used and in lieu of that the rates for males were used for both males and females. We looked at the impact on results and it was fairly small. After discussing with the board, rather than redoing the valuation we would simple note this as an addendum to the valuation to identify the scales properly. The male scale was used for female improvement with the idea that we would go ahead and pick up a correction for this in the following valuation. So this simply represents an amendment to the report disclosing what was actually used in terms of the mortality improvement projections. We ask the committee to approve this as a technical amendment to the report.

Mr. Curran moved to adopt the amendment to the 2015 Valuation Report, and the motion was seconded by Mr. Purpera. With no objections, Senator Peacock said the motion carried.

6. Actuarial Liability Pay-off related to Act 740 of the 2008 Regular Session

Senator Peacock said the committee must vote on this agenda item. Ms. Johnson received a request from Tracey Boyle with the Alcohol and Tobacco Control (ATC) department asking for the payoff amount for the liability created by Act 740 as of June 30, 2016. The calculated payoff is $150,427 which is shown in LASERS valuation approved by PRSAC and the same amount on the projected June 30, 2016, UAL schedules.

Mr. Hall moved to approve the payoff amount for ATC's liability created by Act 740. Representative Pearson seconded the motion and with no objection, the motion was approved.

Continued discussion of:

5. Discussion of Actuarial Assumptions for Louisiana State Employees' Retirement System (LASERS) and Teachers' Retirement System of Louisiana (TRSL)

Ms. Johnson, actuary for LASERS and TRSL, explained that after the last Committee meeting the systems discussed where they are headed with the discount rate. As they indicated at that meeting, they were open to the possibility of lowering the discount rate. At the last board meeting for both systems, the boards adopted a preliminary plan to lower the discount rate in gradual steps, .05% increments to lower from 7.75% to 7.5%. The way that it was specifically presented to the board and approved in their motion was that they would lower it beginning June 30, 2016 by .05%. The valuation for 2016 will be prepared using a discount rate of 7.70% and not impact the contribution rate for fiscal year 2016-17 because that rate has already been approved by PRSAC. We would prepare the projected fiscal year 2017-18 contribution rate using the discount rate of 7.65%. The difference between the 7.75% and the 7.7% for FY2016-17 would fall into the contribution variance. So the amount that the contribution rate would be slightly understated for FY16-17 based on the fact that we would be preparing the valuation using a lower discount rate of 7.7% that would fall into the contribution variance and be collected by the employers over a five year period.

To quantify some of this, looking at the TRSL slide shows the projected changes from lowering the discount rate by .05% increases the employer contribution rate by about .3% and that equates to an employer contribution of about $13.5M for TRSL and the UAL increases by about $143M. These are estimates based on a .05% decrease in the discount rate. She had the breakdown showing what is paid by K-12 and higher education. Higher ed payroll is about 25% of the payroll that pays the UAL payment so that is about $3.4M and K-12 would be about $10.1M. Now remember that is for .05% increments so if we prepare the projected contribution rate for FY16-17 which is the rate we will be bringing to this Committee next year to approve, the second column on her slide shows the contribution rate increase of about .6% or about $27M. For K-12 it would $20.2M and higher education would be $6.8M and the UAL increase of about $285M. So what you will see in the 2016 valuation is an increase of about $143M for the UAL and we will be anticipating another increase in the following year's valuation that we take into account when preparing the FY17-18 projected contribution rate.

Senator Peacock asked what she meant by restated in payment over five years, would it be better instead of a restatement to just start clean and not have to go back, or does that hurt your valuations. Ms. Johnson said the boards felt like they were concerned about bringing another valuation to the Committee based on 7.75% discount rate given that the Committee has indicated an interest in lowering the discount rate. What the board approved was beginning this immediately. Her personal opinion as to whether or not it would be acceptable to wait a year, she would agree with it if the Committee is willing to indicate that they are willing to accept the 2016 valuation prepared with a 7.75% discount rate and a projected contribution rate for FY17-18 based on 7.7% rather than 7.65%. From an actuarial perspective it does not harm the system in any way by waiting a year, these plans are very long time and by waiting one year to do a .05% increment reduction, actuarially is not a problem. The bigger issue is having a plan in place and where do you want to go and the boards have indicated that they want to go to a 7.5% and out of concern for the employers and budgeting impact want to do that on a gradual basis.

Ms. Goodson agreed they should plan and prepare for this in advance and the next year would be the most appropriate time because the local government and the state government has a big budget situation to deal with. Ms. Johnson agreed.

Senator Peacock said everyone would be prepared and know what is going to happen. Ms. Johnson said she can give the similar numbers for LASERS. The impact of a .05% reduction in the discount rate employer contribution rate increases .39%, with the employer contribution increase of $7.5M and a UAL increase of $89M. So if we were to implement the change immediately and prepare the FY17-18 contribution rate with the discount rate of 7.65%, the employer contribution increase would be .77% and the UAL increase of $178M. Ms. Johnson clarified that this is all based only on the impact of changing the discount rate and does not take into account market returns and everything that flows into the 2016 valuation. So she is only estimating that the UAL will increase by $178M, but expect that to be the sole impact of the change in the discount rate. Currently both systems are paying down the UAL because paying principal and not just the interest and we expect to actually pay down by these amounts based on the current schedules without any regards to any new gains and losses. So in the absence of other gains and losses, she expects to continue to see the UAL decrease even with these increases.

Mr. Curran asked Ms. Johnson when she set the rate last time and had the input from the consultants did they cycle through one whole year and has there been any movement from what they are projecting from the last cycle.

Ms. Johnson said she will address separately for TRSL and LASERS. Her recommended range to the LASERS board when she prepared the last experience study was a range of 7.5% to 8.0% for the discount rate. That took into account the gain sharing and all that at the time. So even at that time, she was fine with the 7.5% discount rate. That was developed considering the investment consultant's expected rates of return and they have come down since then.

At TRSL's last board meeting they adopted a new asset allocation so their capital market assumptions have decreased some but they are making some changes in their allocation so you really have to take all that into account, not just where their assumptions have gone.

She is seeing a trend for both of the investment consultants to decrease and indicated to the boards that it is difficult to make these decisions in the current budget situation but she is a little concerned that the investment consultants may continue to decrease their capital market assumptions. She knows this is probably an inevitable need and doing it gradually, if for some reason there is a reverse, and capital market assumptions begin to increase, a gradual plan allows show movement and not to penalize the employers too much. If the market assumptions come down more quickly than this, the boards can revisit it. That is why they were very specific in their motion to call this a preliminary plan to get PRSAC's feedback on it but we feel this is the most reasonable approach at this point in time.

Mr. Curran said his concern is not getting behind the curve because it is pretty tough to catch up. Since Ms. Johnson is saying those expectations dropped to already below and that is consistent with what he finds with his clients as well, therefore it may be a better idea to go with this rather than to have a year delay.

Representative Pearson said Ms. Johnson should have the most intimate knowledge of this system and looking at every aspect. We as legislators are seeing bills for retirement are higher so trying to get a direct answer of what can be done to lower the employer contribution somehow to help offset this. He questioned if they should consider retirement age, retire at higher drop, COLAs, or some other option.

Ms. Johnson said they are already locked for the systems for their UAL schedules, benefits, and all of that and demonstrated by the projections that I prepared for TRSL and that the legislative auditor's office prepared for TRSL and LASERS confirmed that the changes that have already been made are working considerably but in a number of different ways. So the changes that increased the retirement age is beginning to have an impact on the normal cost as more members are coming into the system and have the increased retirement age, we will see the normal cost decrease annually be a fairly small amount but that is already been done by current law.

Representative Pearson asked if there is anything else.

Ms. Johnson said what we expect to see because not readily available to everyone that we do see based on changes already made that the increasing in the UAL payment we are very close to the end of those increasing UAL payments. We are no longer going to have the two large schedules – the OAB and the EAAB increasing at the 5.5-6.0% rates, and very close to increasing at only .6%.

Representative Pearson asked her to study and get back to him. She said that is a much bigger question than can be answered in one minute.

Mr. Henson asked if time for a brief comment from TRSL and LASERS because he would like to hear from both of them.

Mr. Hall asked the difference between the phasing in on this valuation compared to a year from now, if we wait for a year from now are not we just saying that when you do the valuation this year you would use the 7.75% but for the projected rate for the next year, you would use the 7.7%. Ms. Johnson said correct. Mr. Hall said by delaying one year, all you are really doing is eliminating the need to have the contribution.

Ms. Johnson said there would be two things: we would be eliminating the contribution variance and the point for LASERS the .39% annual increase would be delayed for a year. So rather than .77% increase for FY17-18, we would have a .39% increase, and we would not have the contribution variance. So the contribution variance is actually in addition to these numbers, we are looking at a difference of .77% if we implement immediately versus .77% plus a small increase for contribution variance that might have this a little over .8% versus .39%. So .39%, roughly .4%, if we were to wait a year versus if we were to implement it immediately, we would be looking at about .8% - .85%, depends on how it rounds, if talking .8% or .9% for FY17-18. The same numbers for TRSL the contribution variance about .65% and could round to .7% for implementing it immediately versus waiting a year .3%. That's the difference.

Ms. Maureen Westgard, Director of TRSL, said the board has taken this issue obviously very seriously. She and Ms. Rougeou talked following the January 21st PRSAC meeting and decided it was an excellent idea to bring in an outside independent party to take a look at the entire valuation. They both just wanted a fresh set of eyes and it has confirmed exactly where they are. This was not an attempt in any way to make any commentary about the legislative auditor's report but just to do the comparison independently showing where the differences are and why they were there and I think that has been achieved. My board has also been on a parallel path working on asset allocation to do this. Our consultant Aon Hewitt has done an excellent job of providing us with good data to make those decisions and the board did vote on a final allocation. They did the preliminary motion as well to move this forward to move down and it is a difficult decision and as you can imagine while the state system is hard, the teachers system are even more difficult given what is happening in higher education and in K-12. As to the question of the one year delay, I called and spoke with our board chair and our legislative chair who are both here today – that is how seriously they take this issue. We would be okay with that and understand the impacts. The other situation is that the state budget is not really resolved yet. You are once again just as were in January in the middle of this and we understand the impact of the schools. We know that there is a potential $44M cut to them and they are deeply concerned about this. This is the pull and tug of policy setting. That was my question to Shelly too about delaying, asking her as our actuary if she is okay and comfortable with it. What I don't want to happen again, and speaking for the board here, is we don't want to go through another year of this world war three about getting the valuation approved. I just want to be on the record with that. Let's all come to the table here today and talk like adults and look at the bigger picture, not just actuarial nirvana but the real situation in this state with the state's budget and how can you move in the right direction but do so in a very responsible way. We are partners in that and want to be partners in that with you but to have the boards painted as the evil doer of this is just not correct. We have tried to work with you on every piece of legislation to be in the right direction to move back all those things that happened in the past and we are here again as a partner to do that. So that's my statement.

Ms. Cindy Rougeou, Director of LASERS, said that her board is very supportive of reducing the discount rate. We did bring forth this preliminary proposal to show our good faith and will start sooner rather than later, but also understand that there are many other issues at play with respect to the budget and we are sensitive to that. And we have done this as a preliminary motion because we want the feedback of PRSAC. We will not take final action until later in June and so we want your recommendation on this and we will support that.

Ms. Goodson made the motion that we put this in effect starting next year, to give us some time, because we have a regular budget process that we have to go through. My motion would be to put this in effect with the lowering of the discount rate starting probably next January – February when we have to do a new valuation.

Mr. Purpera said at the proper time I would object. I just truly believe we are already lagging behind and need to get on the program if we are going to delay it, then we ought to be adjusting the schedule and making it more aggressive rather than less aggressive.

Mr. Hall seconded Ms. Goodson's motion and said he thinks the important thing is for us to get a process in place and start heading in the right direction. I think consideration for the retirement boards and the budgetary process, I think that this is a good compromise and a good way to approach it.

Senator Peacock said we have a motion and a second, and do have an objection. He asked for any additional discussion.

Mr. Curran asked for clarity on what the motion is. My understanding is that PRSAC does not adopt valuation interest rate, we adopt valuations and I think the boards of these retirement systems have a right to submit the valuation based on their best advice and the legislative auditor's office has a right to submit one too. I think it is appropriate for us to express some sense of where we are going and where our direction might be in terms of accepting one or the other reports, and prejudging in a way. But the reality is we do not have legal authority to dictate a valuation interest rate, but we can do an advisory opinion.

Mr. Westgard said that her board would very much like to have that from PRSAC, an actual statement of their intent.

Ms. Goodson said from our perspective the intent is to put the process in place and move forward starting probably next January when PRSAC has to meet again to develop the ensuing years valuation and retirement valuation.

Ms. Westgard said your action today will help Shelley and our board. We will take final action in our July board meeting and she will begin to develop her valuation then understanding the direction that you have provided and my board provides.

Senator Peacock asked if Mr. Henson or Representative Pearson cared to voice their pro or con on this issue, and on the motion proposed as more of an expression of this committee.

Representative Pearson said I agree that our job is to adopt the valuation and certainly express opinion. Perhaps we could get a unanimous expression from the committee that we would like to see the rate and to give the board the expression from PRSAC that we certainly would like to see go down.

Mr. Henson said the most important thing is to move in the direction and give direction going from 7.75% to 7%. I think we heard from the actuary "no harm, no foul" if we do not do it immediately. We have heard testimony from both directors that their boards would accept that situation, so as long as we express our support for the movement, for the reduction in the discount rate, I think that is the important thing. And I think we can be okay with the delay, but we definitely need to move forward.

Senator Peacock said asked Ms. Goodson to revise her motion to just be the will of this committee to express our direction.

Ms. Goodson moved that the Committee expresses their desire to see both TRSL and LASERS move forward to lowering the discount rate starting with the valuation that would go into effect for FY17-18 on a gradual basis.

Mr. Hall seconded the motion. Senator Peacock said the motion expressed the will of the committee and it has been seconded, and asked if any discussion or objection to the expression. With no objection, the motion is passed favorable.

Ms. Westgard, Ms. Rougeou and Ms. Johnson expressed their gratitude to the Committee.

9. Other Business

Mr. Purpera thanked Senator Peacock for taking the chairman position. No other business was discussed.

10. Adjournment

Mr. Purpera moved to adjourn, and seconded by Ms. Goodson and with no objection, the meeting was adjourned at 9:40 a.m.

Approved by PRSAC: **October 19, 2016**
Date

The video recording of this meeting is available in the House of Representatives' Video on Demand:

http://house.louisiana.gov/H_Video/VideoArchivePlayer.aspx?v=house/2016/jun/0607_16_PRSAC