

MINUTES
BOARD OF TRUSTEES
OF THE LOCAL GOVERNMENTAL EMPLOYEES' RETIREMENT SYSTEM
October 23, 2014

The regular quarterly meeting of the Board of Trustees was called to order at 9:30 a.m., October 23, 2014, by the Chair, State Treasurer Janet Cowell. The meeting was held in the North Carolina Museum of Natural Sciences' Nature Research Center Conference Facility at 111 West Jones Street, in Raleigh.

Members Present

Board members present were: Janet Cowell, John Aneralla, Jerry Ayscue, Lentz Brewer, Randy Byrd, Loris Colclough, Kevin Gordon, and Lou Ann Phillips on behalf of Superintendent June Atkinson, Sally Sandy, and Grady Smith.

Members Absent

The Board members absent were Mike Bradley and Kay Cashion.

Guests Present

The guests attending were: Robert Curran, with the Attorney General's Office; and, Larry Langer and Michael Ribble, with Buck Consultants.

Department of State Treasurer Staff Present

The staff members present were: Steve Toole, Mary Buonfiglio, Thomas Causey, Joan Fontes, Jaclyn Goldsmith, Erica Hinton, Schorr Johnson, Fran Lawrence, Lisa Page, Rosita Sabrosso-Rennick, Kevin SigRist, Vicki Roberts, Anthony Solari, Christina Strickland, Melissa Waller and Sam Watts.

Conflicts of Interest

The Chair asked, pursuant to the ethics rules, about conflicts of interest of Board members. There were no ethics conflicts identified by the Board members.

Adoption of Resolution of Appreciation for the Service of Chipp Bailey

It was moved by Loris Colclough, seconded by Jerry Ayscue, and carried unanimously by the Board to adopt the Resolution for the Service of Chipp Bailey for his tenure on the Board of Trustees' of the Local Governmental Employees' Retirement System.

Approval of the Minutes

It was moved by Kevin Gordon, seconded by Grady Smith, and carried that the minutes of the Board meeting held on July 17, 2014, be approved.

Retirement Systems Division (RSD) Branding, Consumer Segmentation, and Implementation

The Chair recognized Melissa Waller, Chief of Staff, for a presentation on the Department's recent developments on rebranding the Retirement Systems Division's logo. Ms. Waller described how the updated brand would include both the defined benefit plans and the defined compensation plans to increase member awareness of the retirement savings options. Ms. Waller presented that the Department plans to utilize customer segmentation to have a better understanding of its membership and better serve its members in achieving their retirement readiness goals. Lastly, Ms. Waller gave an update on the next steps to submit a Request for Proposal for the Branding and Customer Segmentation in 2014; to work on sharing membership demographics between service providers in the Department; and, to further enhance the Annual Benefit Statement in 2015.

Update from Michael Mebane and John Aneralla on Investment Advisory Committee (IAC) Meeting

The Chair recognized John Aneralla and Michael Mebane, as members of the IAC, for an update on the September 24, 2014 meeting. Mr. Aneralla and Mr. Mebane communicated that they did not have concerns on the investment management of the funds presented at the September 24, 2014 meeting.

RSD Operations Update

The Chair recognized the Retirement Director, Steve Toole, for an update on Operations. Mr. Toole stated that incoming call volume has increased 15.2 percent since last year. He emphasized that the Call Center statistics have vastly improved based on the Deputy Director of Member Service's efforts to hire and train temporary staff to supplement the full-time positions and to increase the space for the Call Center to accommodate additional staffing. As a result, the Call Center is within range of achieving the goal of 80 percent of calls answered in 20 seconds or less, which is the first time the Division has seen that goal reached in years. Mr. Toole stated that refund requests have increased and that the Division has been asking members requesting refunds if they would like the Division to hold payment until January of 2015, so that members will receive the interest on their contributions, based on legislation passed this year. Mr. Toole stated that overpayment invoices have increased by 39.8 percent and that the Division is working on filling the compliance positions granted in the past Short Session of the North Carolina General Assembly. Mr. Toole gave an update on the General Assembly's decision to sunset the Qualified Excess Benefit Arrangement (QEBA), stating that there are 37 potentially affected members and that staff has been contacting these members making them aware that the legislation may impact their retirement benefits if they retire in the near future. Mr. Toole also updated the Board on the Supplemental Retirement Plans membership, contributions status and allocation methods for the past year.

Retiree Supplemental Insurance Products Update

Mr. Toole gave a quick update on the progress of combining the Supplemental Retiree Insurance products with the NC Flex program. He stated that the Retirement Systems Division has been working with NC Flex to submit an RFP for the combined services. Mr. Toole

highlighted that the goal is to reduce premiums and to make a more seamless transition in benefits from active employment into retirement.

Update on 2014 & upcoming 2015 Legislative Sessions

The Chair recognized Anthony Solari, Director of Governmental Relations, for a presentation on the recent 2014 Short Session of the North Carolina General Assembly and what to expect in the 2015 Long Session. Mr. Solari presented the highlights of the 2014 Session, stating that:

- S.L. 2014-100 (Senate Bill 744): The Actuarial Required Contribution (ARC) was met for all the pension systems under RSD and a one percent Cost-of-Living-Adjustment (COLA) was granted to state retirees; the NC 403(b) plan loan was granted to be appropriated from the QEBA with interest; and, the two Fraud, Waste and Abuse compliance positions were secured so that the Department has more resources to monitor occurrences
- S.L. 2014-88 (House Bill 1195): The Anti-Pension Spiking legislation will allow the Department to regulate the few cases where pensions are spiked during the Average Final Contribution (AFC) timeframe used to calculate the member's benefit; Return of Contributions with interest for state and local employees who leave employment within 5 years of hire; and restoration of the vesting period from 10 years to 5 years
- S.L. 2014-64 (House Bill 1034): Significant changes to the administration of the Firefighters' and Rescue Squad Workers' Pension Fund which also allows for age 55 in-service distribution for firefighters' and rescue squad workers
- S.L. 2014-112 (House Bill 1194): Legislation was passed to provide civil immunity for State and Local Retirement Boards

Mr. Solari gave a presentation on the upcoming 2015 Session and stated that the Department will seek to meet the ARC and will recommend COLAs if voted to do so by the Board(s). Mr. Solari explained that it is anticipated that an investment bill will be introduced that will either impact the current sole fiduciary role or change to a board governance structure. Lastly, Mr. Solari stated that this upcoming Session may involve debates on the Defined Benefit Plan versus the Defined Contribution Plans options.

Board Best Practices

The Chair recognized Ms. Waller for a presentation on the Department's implementation of Board Best Practices. Ms. Waller presented that it has been an initiative of the State Treasurer to establish Board Best Practices across all of the Boards under the Department. Ms. Waller stated that the Department worked on an on-going basis to make enhancements to the Board meeting rooms to address the Board members' needs and to develop materials that best prepare them to carry out their responsibilities. She announced that the IAC recently participated in a survey, conducted by an independent firm, to evaluate the administration of the Committee which included assessing the materials and the work of the Investment Advisory staff. Ms. Waller stated that the Department plans to undertake a similar evaluation of other Boards in the Department during 2015, which will include the State and Local Boards of Trustees.

Government Accounting Standards Board (GASB) Pension Accounting Standards Update

The Chair recognized Fran Lawrence, Chief Financial Officer, for a presentation on the implementation of the new GASB accounting standards. Ms. Lawrence presented that the GASB 67 implementation was included in the June 30, 2014 submittal of the Comprehensive Annual Financial Report (CAFR). The implementation discloses the Net Pension Liability or Net Pension Asset by pension plan for the first time. She gave a status of GASB 68 and stated that implementation is in process and that there are not any significant additional disclosures at the Pension Plan level, but there are new items to be recorded by employers for the fiscal year ending June 30, 2015. Ms. Lawrence also gave an update on GASB 67 and 68 Audit stating that the June 30, 2014 CAFR Audit is in process and the Office of State Auditor (OSA) selected a sample of employers from the Local Governmental Employees' Retirement System (LGERS) and the Teachers' and State Employees' Retirement System (TSERS) for census data testing. She mentioned that local auditors have been instructed by OSA and the State and Local Government Finance Division to provide assurance related to specific data elements provided to the retirement systems. Also, a separate audit opinion will be provided by OSA on the GASB 68 tables that allocate the Net Pension Liability or Net Pension Asset for the three cost-sharing plans.

Anti-Pension Spiking Contribution-Based Benefit Cap (CBBC)

The Chair recognized Mr. Toole for a presentation on the recent legislation that established an anti-pension spiking CBBC for members retiring on or after January 1, 2015. Mr. Toole explained the Department's definition of pension spiking and stated that Session-Law 2014-88 (House Bill 1195) "Fiscal Integrity/Pension-Spiking Prevention" is based on the recommendations by Buck Consultants on the Fraud, Waste, and Abuse report delivered to the Board in October, 2013.

Mr. Toole presented how the current unforeseen liabilities are shared by all employers of the Retirement System when a member's pension is spiked during the member's Average Final Compensation (AFC) used in the benefit calculation at retirement. After January 1, 2015, based on the legislation the employer is required to pay the cost of the unforeseen liability; or if hired after January 1, 2015, the employer or employee must cover the liability from the pension spike. He specified that any member retiring with an AFC less than \$100,000, adjusted annually, would not be subject to review for pension spiking. He set forth scenarios to illustrate how a member's situation would be analyzed for pension spiking to clarify how the Department would implement the legislation into effect. Mr. Toole introduced the concept of the CBBC factor which is used in the formula to determine the maximum benefit an employee can earn without causing a spike to their pension. Mr. Toole handed the presentation off to Buck Consultants to present the logistics of setting the factor.

Larry Langer and Michael Ribble, with Buck Consultants, presented the analysis of Session Law 2014-88 and stated that the Board of Trustees has been designated to adopt a CBBC factor recommended by the actuary. Based on the legislation, no more than three-quarters of one percent (0.75 percent) of retirement allowances are expected to be capped. Mr. Langer presented factors

and the corresponding expected percent of members that would reach that cap for the TSERS and LGERS plans. Mr. Langer stated that the analysis of the factors is based on the December 31, 2012 valuations and the prior experience study conducted in 2010. He advised that if the Board finds the factor chosen did not meet or exceeded the .75 percent threshold, the Board can adjust the factor after the next experience study is presented, which is scheduled for late 2015.

It was moved by Jerry Ayscue, seconded by Lou Ann Phillips, and carried unanimously by the Board that the factor of 5.1 be set for the Local Governmental Employees' Retirement System.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2013 by Buck Consultants for the Death Benefit Plans

Mr. Langer and Mr. Ribble presented the findings in the Death Benefit Plans actuarial valuation. Mr. Langer reminded that beginning July 1, 2012, the Board granted one, two, and three year contribution holidays to employers based on number of years each employer has contributed to the LGERS death benefit plan and that the contribution holidays would be ending this year. He stated that as of the December 31, 2013 actuarial valuation, the death benefit plan is in surplus of \$53.9 million. Mr. Langer updated that the Retirees' Contributory Death Benefit Plan reported a deficit of \$35.2 million. He explained that benefits payable under the Retirees' Contributory Death Benefit Plan are supported entirely by the contributions of the participants and the investment earnings on the contributions. He suggested for a review of the plan provisions and contribution rates to evaluate adjusting the projected shortfall.

Mr. Langer gave an update on the Separate Insurance Benefits Plan, stating that about \$16.5 million was transferred out of the Separate Insurance Benefits Plan to reimburse employer paid State Health Plan premiums made on behalf of state law enforcement officers and to reimburse employer paid contribution rates for the State Health Plan based on the reported compensation of state law enforcement officers. The diversion of these funds decreased the surplus of the Separate Insurance Benefits Plan from \$61.5 million as of the December 31, 2012 valuation to surplus of \$56.8 based on the December 31, 2013 valuation. Mr. Langer stated that a negative return of 4.1 percent from the fixed income portfolio also impacted the December 31, 2013 valuation. He stated to the Board that if the transfer amounts of \$16.5 million continue beyond fiscal year ending June 30, 2015, the fund could be depleted in 2016 and is dependent on bond market returns subsequent to the most recent valuation.

It was moved by John Aneralla, seconded by Greg Grantham, and carried by the Board that the Death Benefit Plans actuarial valuation be accepted.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2013 by Buck Consultants for the Local Governmental Employees' Retirement System (LGERS)

Mr. Langer and Mr. Ribble presented the findings in the LGERS actuarial valuation. Mr. Langer reviewed the purpose of the annual actuarial valuations and the valuation process. He presented that the results differed from the prior year due to market value returns of 12.21 percent compared to 7.25 percent assumed rate of return, increase in payroll of 2.3 percent compared to the 3.0 percent assumed increase, and recent legislation signed into law that included return of contributions with interest for all members prior to vesting requirement. These

factors resulted in a lower employer required contribution rate of 6.52 percent for fiscal year ending June 30, 2016 compared to the 7.11 percent in the December 31, 2012 baseline projection and a lower employer contribution rate of 7.0 percent for fiscal year ending June 30, 2016 for law enforcement officers compared to the 7.59 percent in the December 31, 2012 baseline projection. Mr. Langer reported that the funded ratio on an actuarial basis remained at 99.8 percent at the December 31, 2013 valuation.

It was moved by Lou Ann Phillips, seconded by Grady Smith, and carried by the Board that the LGERS actuarial valuation be accepted.

Presentation by the Consulting Actuary on the Stabilization of Employer Contribution Rates in the Local System

Mr. Langer and Mr. Ribble presented the current funding policy. Mr. Langer explained how the actuarial methods used allow for more flexibility in paying the costs of the Retirement System and how the funding policy selected by the Board of Trustees should strike a balance between contributions that are stable from year to year but also satisfy the actuarial needs of the Retirement System. He stated that the actuarial methods used for the North Carolina Retirement Systems are well within the recommendations in the accounting standards under GASB 25 and 27. He also defined the volatility in the System in response to the market downturn in 2008 when contributions based on valuations began to increase after years of stabilization in order to sufficiency meet the ARC. He stated while stable contribution funding would not eliminate the need for rising contributions in down markets, it would remove the need for annual contribution increases and the current projected rate decreases make this an opportune time to consider a Stable Contribution Funding Policy. Mr. Langer stated that the Board, depending on the final solution, may need to seek legislative authority, but a stable funding contribution policy can be constructed to achieve stable and predictable contribution levels and would maintain the actuarial integrity of the Retirement Systems. It was requested by the Board that Buck Consultants present projections of the stable contribution-funding policy in the January, 2015 Board meeting.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2013 by Buck Consultants for the Register of Deeds' Supplemental Pension Fund

Mr. Langer and Mr. Ribble presented the findings in the Register of Deeds' Supplemental Pension Fund actuarial valuation. Mr. Langer presented that the funded ratio increased slightly to 192.8 percent in the December 31, 2013 valuation compared to the funded ratio of 191.3 percent as of the December 31, 2012 valuation. This results in the Annual Required Contribution (ARC) maintaining at 0.0 percent.

It was moved by Randy Byrd, seconded by Jerry Ayscue, and carried by the Board that the Register of Deeds' Supplemental Pension Fund be accepted.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2013, by Buck Consultants for the Firefighters' and Rescue Squad Workers' Pension Fund (FRSWPF)

Mr. Langer and Mr. Ribble presented the findings in the FRSWPF actuarial valuation. Mr. Langer presented that results differed from prior year due to market value returns of 12.42 percent

compared to 7.25 percent assumed rate of return; recent legislation signed into law on the in-service distribution at age 55 with twenty years of service; and, the adjustments to the actuarial assumptions intended to estimate the data for lapsed members. These factors resulted in a higher funded ratio of 88.3 percent as of December 31, 2013 compared to 83.9 percent in the June 30, 2012 valuation. Mr. Langer reported a lower ARC of \$13,240,522 for fiscal year June 30, 2016 compared to ARC of \$14,620,362 for fiscal year ending June 30, 2014.

It was moved by Kevin Gordon, seconded by Randy Byrd, and carried by the Board that the FRSWPF actuarial valuation be accepted.

Full Data Audit – Phase 2 Preliminary Findings on the FRSWPF

Mr. Langer and Mr. Ribble presented the findings on Phase 2 of the Full Data Audit of the FRSWPF being conducted by Buck Consultants. He reviewed the Department's purpose for retaining Buck Consultants to assess the current assumptions on lapsed members returning to active service and becoming vested in their benefit. Mr. Langer updated that Buck Consultants focused on the 13,500 of the 40,000 members of the Plan who did not receive a year of service credit as of the last actuarial valuation for purposes of the data audit. He reported that Buck Consultants has been onsite researching and has so far reviewed 6,500 of the 13,500 records to date. Based on the review of the population as of the Phase 2 findings, Buck expects to remove at least 25 percent of the 13,500 lapsed members. If applied to the entire population, this represents over 3,000 members who are not expected to return to active membership (this is an increase from Buck Consultant's initial expectation to remove 2,500 members). Mr. Langer stated that it is reasonable to continue to assume fiscal year ending 2015 contributions will be reduced by \$2.2 million and including a \$1.7 million reduction from the current appropriation. Mr. Langer reported that final results are expected to be available by first quarter 2015.

Local Units Applying to Participate in the Local Governmental Employees' Retirement System

Mr. Toole presented Avery County Fire Commission and Duplin County Tourism Development Authority as employers applying for participation into the Local Governmental Employees' Retirement System. It was moved by Loris Colclough, seconded by John Aneralla, and carried unanimously by the Board to approve Avery County Fire Commission and Duplin County Tourism Development Authority for participation as an employer in the Local Governmental Employees' Retirement System, with an effective date of January 1, 2015.

Adjournment

There being no further business, Kevin Gordon moved for adjournment of the meeting, which was seconded by Lou Ann Phillips, and carried. The meeting adjourned at 2:40 p.m.

CHAIR

SECRETARY