MINUTES
BOARD OF TRUSTEES
OF THE TEACHERS' AND STATE 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

The Board members present were: Janet Cowell, John Aneralla, Lentz Brewer, Jack Brooks, Loris Colclough, Van Dowdy, Greg Grantham, William Grey, Alberta Hall, Michael Jacobs, Michael Mebane, and LouAnn Phillips on behalf of Superintendent June Atkinson.

Members Absent

No Members were absent.

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.

Approval of the Minutes

It was moved by Michael Mebane, seconded by Lentz Brewer, and carried that the minutes of the Board meeting held on July 17, 2014, be approved.

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 Benefits 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 Services' 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 to make 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 has 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 Board 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 or the employee can choose to receive a reduced retirement benefit amount. 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. 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 John Aneralla, seconded by Loris Colclough, and carried unanimously by the Board that the factor of 4.8 be set for the Teachers' and State 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 Teachers' and State Employees' Retirement Systems (TSERS)

The Chair recognized Mr. Langer and Mr. Ribble for a presentation on the findings on the TSERS 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 the 7.25 percent assumed rate of return, increase in covered payroll of 0.5 percent was less than the 3 percent assumed increase; and, recent legislation signed into law for the one percent COLA, return of five-year vesting for active members, and return of contributions with interest were all included in the valuation analysis. These factors resulted in a slightly higher funded ratio of 94.8 percent as of the December 31, 2013 valuation compared to the baseline projection of 93.9 percent. The employer required contribution rate for fiscal year ending June 30, 2016 is 8.69 percent and is less than the 9.15 percent in the baseline projection.

It was moved by Loris Colclough, seconded by Michael Jacobs, and carried by the Board that the Teachers' and State Employees' Retirement System 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 Consolidated Judicial Retirement System (CJRS)

Mr. Langer and Mr. Ribble presented the findings of the CJRS actuarial valuation. Mr. Langer presented that the results differed from prior year due to a market value return of 12.19 percent compared to the 7.25 percent assumed rate of return; increase in payroll of 0.3 percent was less than the 3 percent assumed increase; and, recent legislation signed into law for the one percent COLA, return of five-year vesting for active members, and return of contributions with interest were all included in the valuation. These factors resulted in a slightly higher funded ratio of 92.3 percent as of the December 31, 2013 valuation compared to the 91.2 percent in the December 31, 2012 valuation. The employer required contribution rate for fiscal year ending June 30, 2016 is 26.37 percent and is slightly less than the 26.55 percent required for fiscal year ending June 30, 2015.

It was moved by Michael Mebane, seconded by Lentz Brewer, and carried by the Board that the CJRS 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 Legislative Retirement System (LRS)

Mr. Langer and Mr. Ribble presented the findings in the LRS actuarial valuation. Mr. Langer presented that the results differed from prior year due to a market value return of 12.2 percent compared to the 7.25 percent assumed rate of return; the increase in payroll was 2.0 percent and less than the 3.0 percent assumed increase; and, recent legislation signed into law for the one percent COLA, and return of contributions with interest were included in the valuation. The factors resulted in a slightly lower funded ratio of 119.4 percent for December 31, 2013 compared to the 123.3 percent from the December 31, 2012 valuation. Mr. Langer said the lower funded ratio was due to more retirements processed than expected. Mr. Langer reported that the employer contribution rate is 1.80 percent for fiscal year ending June 30, 2016, higher than the 0.00 percent for fiscal year ending June 30, 2015.

It was moved by Loris Colclough, seconded by Lou Ann Phillips, and carried by the Board that the LRS 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 Disability Income Plan of North Carolina (DIPNC)

Mr. Langer and Mr. Ribble presented the findings in the DIPNC actuarial valuation. Mr. Langer presented that reported compensation and valuation compensation remained flat to the December 31, 2012 valuation results. These factors resulted in an unchanged ARC of 0.41 percent for fiscal year ending June 30, 2015 and June 30, 2016.

It was moved by John Aneralla, seconded by Michael Mebane, and carried by the Board that the Disability Income Plan of North Carolina 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 North Carolina National Guard

Mr. Langer and Mr. Ribble presented the findings in the North Carolina National Guard actuarial valuation. Mr. Langer reviewed the 12 year amortization period and the GASB 25/27 changes to the normal cost and accrued liability. Mr. Langer reported a slightly higher funded ratio of 73.8 percent for December 31, 2013 compared to 73.3 percent in the December 31, 2012 actuarial valuation and that the appropriation for fiscal year ending June 30, 2015 is $6,039,274.

It was moved by John Aneralla, seconded by Van Dowdy, and carried by the Board that the North Carolina National Guard actuarial valuation be accepted.

Implementation of Legislative Budget Directive to Provide for 403(b) Supplemental Plan Start-up Costs from State System QEBA

The Chair recognized Mr. Toole for a presentation on the transfer from the State System's QEBA to the 403(b) Supplemental Retirement Plan as directed by the North Carolina General Assembly in Section 35.15A of the 2014 Appropriations Act (Senate Bill 744). Mr. Toole explained that the transfer would provide the startup costs to administer the statewide 403(b) plan. He stated that under the terms of the loan, the 403(b) plan would repay the QEBA when the balance in the 403(b)'s administrative account exceeds $250,000 and that the loan will be repaid at an interest rate set by the Board of Trustees.

It was moved by John Aneralla, seconded by Michael Jacobs, and carried unanimously by the Board to set the interest rate at 7.25 percent for the loan from the QEBA to the 403(b) plan.

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 presented that the Death Benefit plans for the TSERS has a surplus of $16.7 million and a set contribution rate of 0.16 percent. 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.

State System Adjournment

There being no further business, Michael Jacobs moved to adjourn the meeting, which was seconded by Lentz Brewer, and carried. The meeting adjourned at 1:40 p.m.

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CHAIR

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SECRETARY