March 13, 2012
Minutes #478

Minutes of the Board of Trustees' Meeting -1-

Call to Order: Chairman Pinard called the meeting to order at 8:35 a.m.

Present: Trustees: Chairman Pinard, Bill Sanders, Michael Woitkowski, Mayor Gatsas. Dick Molan arrived at 8:37 a.m. and Dianne Mercier departed the meeting at 9:30 a.m.

MECRS Staff: Gerard Fleury, Sandi Aboshar and Suzanne Wilson

Absent: Paul Porter

In Attendance: Chief Actuary, David Kausch from Gabriel, Roeder, Smith & Co. and Attorney John Rich of the McLane Law Firm. Also, via conference call, Mr. Ken Alberts from Gabriel, Roeder, Smith & Co.

Approval of the Minutes of the Previous Board Meeting:

Trustee Woitkowski moved to approve the minutes of the meeting of February 21, 2012, seconded by Trustee Sanders and passed unanimously by all trustees present.

Approval of the Immediate Meeting Agenda:

A motion was made by Trustee Sanders to approve the immediate meeting agenda, seconded by Trustee Woitkowski, and passed unanimously by all those trustees present.

New Business:

Presentation and Review of the Annual Actuarial Valuation – Mr. David Kausch, Chief Actuary from Gabriel, Roeder, Smith & Co., introduced himself and noted that Mr. Ken Alberts, also of GRS, will be linked into the meeting via conference call to review the actuarial valuation results for 2011 and to answer any questions that the board may pose prior to the formal acceptance of the valuation. An attempt to link Mr. Alberts was unsuccessful due to technical difficulties and so Mr. Kausch proceeded with the GRS presentation.

First, Mr. Kausch began by stating that the funding objective of a Retirement System is to establish and receive contributions which when expressed as percents of active member payroll, will remain approximately level from year to year and will accumulate sufficient assets over each member's working lifetime to finance promised benefits throughout retirement without putting an undue burden on the contributing employer and taxpayers.

Minutes of the Board of Trustees' Meeting -2-

Beginning with page A-2 of the valuation, Summary Statement of System Resources and Obligations, which identifies both pension and health trusts values, Mr. Kausch gave a detailed explanation of two charts entitled, "Present and Expected Future Resources" and the "Actuarial Present Value of Expected Future Benefit Payments." He noted the actuarial value of System assets of slightly over $140 million for pensions and $5 million for health. He further noted that the trustees might want to consider an optional alternative smoothing method which he said would be discussed later in the meeting.

Mayor Gatsas questioned Mr. Kausch about the previous years' employer contribution rate and so Mr. Kausch directed the trustees to page A-7, Contribution Rate Reconciliation, and he pointed out where the composite rate for pension and health was listed at 18.58%.

Remaining on the Contribution Rate Reconciliation, Mr. Kausch cited this year's proposed employer contribution rate breakdown of 18.75% for the pension trust and 0.97% for the health trust, for a total employer rate of 19.72%.

Trustee Sanders asked about the reported Experience Loss of 0.71% on the reconciliation chart, most of which was on the pension side, and he asked Mr. Kausch about the nature of the loss. Mr. Kausch replied that the biggest portion of the loss was attributed to investment losses that are now being recognized.

Elaborating further on the experience loss, Mr. Kausch directed the trustees to turn to page A-6 of the valuation, Derivation of Experience Gain (Loss). He stated that the chart indicates a derivation of the total dollar amount of the loss, $6,036,164 for pension benefits and $401,422 on the health side. Overall, the pension funding status decreased from 62.4% to 61.6% while the health status rose from 34.6% to 37.4%.

Turning to page A-4 of the report, Development of Funding Value of Assets, Mr. Kausch explained that the funding value of assets recognizes assumed investment income fully each year. Differences between actual and assumed investment income are phased in over a closed 5-year period. During periods when investment performance exceeds the assumed rate, the Funding Value of Assets will tend to be less than the Market Value. During periods when investment performance is less than the assumed rate, the Funding Value of Assets will tend to be greater than the Market Value. He explained that phasing in the entire past asset gains and losses for 2011, results in a total loss of $6.1 million.

Trustee Sanders then asked how those numbers compare to what the MECRS investment consultant would be reporting.

Mr. Kausch explained that GRS's calculation is different from that of NEPC. GRS is weighted by cash flow timing while NEPC measures investment performance.

Trustee Sanders asked Mr. Fleury to provide some kind of reconciliation to what NEPC reports, so that he may compare it to the GRS valuation.

Trustee Sanders stated that the MECRS experience loss is more than he anticipated.

Carrying the loss forward to 2012 valuation, Mayor Gatsas asked Mr. Kausch for his professional opinion as to what the System could expect going into 2013.

Mr. Kausch explained that it is difficult to project the market value cash flow and the non-investment cash flow moving forward.

Mr. Kausch then reminded the trustees that he does have an alternative smoothing method, as another option, which he would discuss later in the meeting.

Returning to page A-7, Mr. Kausch again addressed the employer contribution rate and he provided details as to how that rate is computed for various lines in the contribution rate reconciliation table.

Trustee Sanders asked about the number of participants electing the health benefit and based on the recent valuation, he asked, how many members are assumed to elect that benefit.

Referring to page A-11, Mr. Kausch explained that beginning with the December 31, 2007 valuation, GRS set the utilization assumption at 60%. There is very little historical data, but it appears that over the last five years only about 50% have elected to receive the subsidy. He stated that GRS will continue to monitor health subsidy utilization history as it is generated.

Chairman Pinard noted that despite lower than expected utilization, that last year's health contribution rate of .87% is expected to increase to .97%. The trustees discussed the Health Trust as well as the Comparative Statement of past valuation results.

Mr. Kausch then offered to explain the option for an alternate smoothing method so that the trustees' might consider its applicability.

He stated that the alternate smoothing method assumes that the System will meet its actual assumed rate of return of 7.5%. The difference is, it is giving the System another 5 years to amortize the $6 million loss which must presently be recognized under the method in place.

After lengthy discussion by the trustees, it was agreed that the actuary should re-calculate the funding value as well as the funding value using the alternate method, and to also provide those results using lower assumed rates of return of 7.25%, 7% and 6%.

Mr. Kausch commented that Mr. Alberts is concerned that under the current method MECRS may be subjected to more volatility without adopting the re-smoothing method. He also noted that Plans across the country are lowering or are considering lowering their assumed rates of return.

Mr. Fleury made a second and successful attempt to conference in Mr. Ken Alberts of GRS.

Mr. Kausch recapped discussion thus far to Mr. Alberts regarding the alternative smoothing method, spreading out the gains and losses. Trustee Sanders and Trustee Mercier both expressed their concern with deferring the losses through smoothing as well as the possibly over optimistic 7.5% rate of return assumption. Mr. Kausch went on to say that Trustee Sanders has requested a review of what the impact to the System would be under alternate investment return assumptions in conjunction with reviewing the changing of the smoothing method, specifically asking for lower assumed rates of return, 7.25% and 7% and that the Mayor requested a 6% return assumption.

Mr. Alberts explained that in order to complete the board's request in time for the next meeting that he would only be able to run the funding value for two rates and he recommended using the 7% and 6% assumed rates of return.

Mayor Gatsas asked Mr. Alberts to predict what those assumptions would produce.

Mr. Alberts responded that as a rule of thumb, a one percent interest rate change would have approximately a 20% change in the cost but he explained that that does not necessarily translate into a change of that magnitude in the contribution rate. The contribution rate would be more than that because of leveraging, the liability would grow by 20%, but the assets would not change, so the unfunded liability would grow more.

The trustees continued to discuss different scenarios at length and the affect that each of the variables would have on the Plan.

Mr. Alberts suggested that the board may also want to consider accelerating the 5-year Experience Study after the adoption of the 2011 valuation. He noted that the last Study was done 3 years ago. Repeating the study now would provide GRS with a solid 3 years of experience to work with. Then the board could revert back to conducting an experience study every 5 years.

At this point, the board decided to schedule a special meeting at the end of the month and to have both the System's actuary and the System's investment consultant in attendance in order to get a better understanding of what the Plan is dealing with, before adopting any employer contribution rate.

Mr. Fleury stated that he would coordinate the March meeting with GRS and NEPC and that he would be contacting the trustees as to the date and time of the special meeting.

It was moved to table the adoption of the System's 2011 Annual Actuarial Valuation, seconded by Trustee Sanders and passed by all those trustees present.

Previous Business:

Reconsideration of DRAFT Administrative Rule 7 - Moved by Trustee Molan to remove the Administrative Rule 7 from the table, seconded by Chairman Pinard and passed unanimously by all those trustees present.

Mr. Fleury recapped the discussion on Admin. Rule 7 from the February Board Meeting and reminded the Board that he has been directed to work up examples of the new rule by applying it retroactively using historical data from valuations so that everyone could see what might have transpired had the rule been in effect. The results of Mr. Fleury's efforts had been distributed to the trustees at the start of the meeting.

It was then moved by Trustee Sanders to re-table, DRAFT Administrative Rule 7 for the trustees' further consideration, seconded by Trustee Molan and passed unanimously by all those trustees present.

Trustee Sanders then asked when the MECRS board traditionally considers whether a COLA will be awarded. Mr. Fleury replied, the retiree COLA is customarily considered beginning in May and concluded in June so that when COLAs are granted, they can become effective in July without the need for a retroactive payment.

Chairman Pinard recessed the meeting for attorney/client privilege session at 9:52 a.m.

Chairman Pinard reconvened the meeting at 10:40 a.m.

New Business:

Ordinary Disability Request from John Gillis – Mr. Fleury referred the trustees to a recommendation included in their agenda packets and stated that Mr. Gillis has met all the requirements for an Ordinary Disability. In summary, he stated that it is his recommendation that the disability benefit request be approved.

It was moved by Trustee Molan to grant the Ordinary Disability request for Mr. John Gillis, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Consent Agenda:

It was moved by Trustee Molan to accept the Consent Agenda, seconded by Trustee Sanders and passed unanimously by all those trustees present.

Report of the Executive Director:

Issues with MECRS Web Site Discovered – Mr. Fleury began by reporting that a complaint from a client helped to discover that a functionality problem existed on the MECRS web site. Anyone who uses the site is able to click on a "Web Support" button to request technical assistance by simply providing their name and a contact email address. For reasons not clearly understood at the time, the mailbox which receives requests for assistance ceased to forward messages to MECRS staff for resolution. After the problem was discovered, an initial backlog of requests was resolved and the problem with the forwarding mechanism was fixed.

No Financial Statement This Month - Next, Mr. Fleury reported that as usual for this time of year, the production of fiscal year 2012 monthly statements is not possible due to the delay in receiving and posting the final December 31, 2011 investment values. At the present time, most of the values have been determined and next month, the trustees should see a resumption of monthly statements for 2012.

Report of the Investment Committee:

Committee Chairman Molan reported that the Investment Committee had held a meeting the day before and that Trustee Sanders and Trustee Mercier had been in attendance. Also, present were NEPC Representatives, Mr. Kevin Leonard and Mr. Sebastian Grzejka.

The committee listened to a presentation by Mr. James Raisides and Ms. Nicole Dutra-Grinnell, Partners of TA Associates. They provided the trustees with a fiduciary education session on value added, closed end real estate funds.

Committee Chairman Molan stated that their presentation was excellent and that the representatives were able to answer all questions posed by the committee members as well as providing the committee with their philosophy and detailed investment strategy.

Also, Trustee Molan noted that NEPC has been asked to schedule two more real estate managers for interviews in April. Following those interviews, the Investment Committee would likely, make a recommendation to adding an additional real estate manager to the MECRS portfolio.

Motion to Adjourn:

Having completed all of the items of business for the day, Chairman Pinard entertained a motion to adjourn. Trustee Molan moved to adjourn at 10:55 a.m. seconded by Trustee Sanders and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard E. Fleury
Executive Director