

Sinking Fund Commission - October Meeting
October 1, 2019

CITY OF PHILADELPHIA
SINKING FUNDS COMMISSION
Tuesday, October 1, 2019

- - -

LOCATION: Two Penn Center Plaza
16th Floor
Philadelphia, Pennsylvania

REPORTED BY: Amy Marzario,
Court Reporter

PRESENT: DONN SCOTT, CHAIRMAN
AL JOHNSON
JERRY MANDIS
CHRISTOPHER DIFUSCO
ALEX GOLDSMITH
MARC AMMATURO
REBECCA RHYNHART
KELLAN WHITE
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1 MR. SCOTT: It's my pleasure
2 to call this meeting of the Sinking Funds to
3 order. The first order of business is the
4 approval of the minutes from July 11, 2019.
5 Is there a motion?

6 MR. DUNBAR: So moved.

7 MR. SCOTT: Is there a
8 second?

9 MS. RHYNHART: I can second
10 it.

11 MR. SCOTT: The motion has
12 been made and properly seconded. All those
13 in favor?

14 MR. DUNBAR: Aye.

15 MR. SCOTT: Okay. The second
16 order of business is the annual actuarial
17 presentation so I'll turn it over to Mr.
18 Johnson.

19 MR. JOHNSON: Okay. Thank
20 you. Good to be here, everybody. I'm Al
21 Johnson from Aon Corporation. Alongside me
22 is Jerry Mandis who is a colleague of mine
23 who works on the PGW account with me.

24 So this is our annual actuarial

1 evaluation report for PGW's pension plan.
2 Its purpose is to provide you a snapshot of
3 the pension liabilities of the plan as of
4 July 1, 2019, the cash funded position of
5 the plan as of that date, and the cash
6 funding requirements for the July '19
7 through June 30th plan here based on the PGW
8 policy -- the funding policy that PGW has
9 adopted in the past. So that's what we're
10 going to review here today.

11 Please flip over to page 1. I
12 might jump around a little bit in this
13 report so forgive me. Here is some basic
14 information on the plan -- demographics of
15 the plan from July 1 of '18 and July 1 of
16 '19 as a snapshot.

17 So the first line is active
18 participants. We had a decline in active
19 participants from last year to this year.
20 This has been a trend that this number has
21 been in slightly decline as we go forward so
22 this is going to be expected in the new
23 hires. The new hires from PGW have the
24 choice of going into the defined

1 contribution plan or the defined benefit
2 plan.

3 So what we're seeing is about four
4 -- this year, we saw 55 percent joined the
5 DB plan -- what I call the defined benefit
6 plan, DB plan, and the other 45 percent
7 joined the defined contribution plan. So
8 for every 100, 55 went in here and 45 went
9 into defined contribution.

10 MS. RHYNHART: And why are --
11 are the employees -- how is the union
12 directing the employees? Is the union
13 directing the employees to -- recommending
14 one or the other?

15 MR. CAWLEY: Not to my
16 knowledge.

17 MS. RHYNHART: Okay.

18 MR. JOHNSON: I would imagine
19 that the union is probably encouraging their
20 new members to join the defined benefit plan
21 just because of --

22 MS. RHYNHART: That's what I
23 was thinking.

24 MR. JOHNSON: -- the security

1 that it provides long term where the defined
2 contribution plan, the investment risk lies
3 with the employees.

4 MR. LEONARD: Yes, I would
5 confirm what Al is saying.

6 MS. RHYNHART: But it's
7 interesting to me that 45 percent are not
8 joining the defined benefit. Is that
9 because they don't plan to stay for that
10 long? It's interesting.

11 MR. LEONARD: I don't know if
12 whether their intention is whether or not
13 they're going to stay. I know non-union
14 employees are more leaning towards the
15 defined contribution plan whereas
16 union-covered employees are leaning more
17 towards the defined benefit plan for the
18 pension plans.

19 MS. RHYNHART: What's your
20 breakdown for union and non-union?

21 MR. LEONARD: Roughly, we
22 have about 1,000 to 1,100 union-covered
23 employees with the remainder being
24 non-union. So we roughly have about 400 to

1 500 non-union employees roughly.

2 MS. RHYNHART: Okay.

3 MR. DIFUSCO: Did that number
4 change? I feel like for some reason within
5 the last couple years it was more like
6 two-third, one-third in prior reports from
7 Tom. So has that number fluctuated at all?

8 MR. JOHNSON: That number
9 will fluctuate year after year. I mean, you
10 could have -- like any other actuarial
11 assumption, you're going to have ups and
12 downs on it. You're never going to quite
13 hit it.

14 MR. DIFUSCO: Right.

15 MR. JOHNSON: We assume 50
16 percent on a long-term basis if that's what
17 it's going to be. So our 55/45 is sort of
18 in a range. Maybe next year that floats
19 around. That's the other way.

20 MR. DUNBAR: Why are you
21 assuming 50 percent?

22 MR. JOHNSON: Just based on
23 the experience that we've seen in the plan.
24 Roughly, that's where the split is coming.

1 MR. DUNBAR: Do you know if
2 there's an added benefit to joining the
3 defined contribution plan? Is there an
4 added benefit; higher matching or something?

5 MR. LEONARD: No, it's
6 actually the reverse. Any employee that
7 chooses the defined benefit will have to
8 contribute 5.5% of their salary.

9 MS. RHYNHART: Right. But
10 does that --

11 MR. LEONARD: Or, excuse me,
12 up to 6% of their salary.

13 MS. RHYNHART: Does PGW match
14 that?

15 MR. LEONARD: No, we don't
16 match that 5%.

17 MR. JOHNSON: No, I think he
18 means on the defined -- the benefit plan.

19 MS. RHYNHART: Oh, okay.

20 MR. LEONARD: On the defined
21 benefit -- so if an employee elects a
22 defined benefit plan or selects a pension
23 plan, they have to contribute up to 6% of
24 their salary towards the pension plan. If

1 they define -- or elect to choose a defined
2 contribution, PGW will contribute I think
3 5.5% to their 401k.

4 MR. DUNBAR: As a match or
5 just a --

6 MR. LEONARD: Up to 5.5%.

7 MR. DUNBAR: As a match?

8 MR. LEONARD: Yes.

9 MR. DUNBAR: Okay.

10 MR. LEONARD: So there's more
11 incentive for the employees to elect the
12 defined contribution plan than there would
13 be the defined benefit.

14 MR. DUNBAR: Okay. That's
15 what I'm trying to get at. That would
16 explain it.

17 MS. RYHNHART: So the union
18 is saying go defined benefit because you
19 have the guarantee and then --

20 MR. LEONARD: Right.

21 MR. DUNBAR: In this
22 assumption, 45 is not joining the defined
23 benefit plan but does that mean they
24 actually joined the defined contribution

1 plan or they're just not -- 'cause you can
2 have a percentage of them that aren't doing
3 anything?

4 MR. LEONARD: One or the
5 other.

6 MR. DUNBAR: You have to do
7 one or the other?

8 MR. LEONARD: Yes.

9 MR. JOHNSON: For our
10 purposes, we just want to know how many
11 people are coming into the defined benefit
12 plan. If they don't join, then that's fine.

13 MR. DUNBAR: I was just
14 wondering. So they have to do one or the
15 other?

16 MR. LEONARD: One or the
17 other. And an employee who joins PGW has up
18 to 30 days to select either defined benefit
19 or defined contribution. If an employee
20 does not make a selection after the 30-day
21 period, the employee will be automatically
22 enrolled into the defined contribution plan.

23 MR. DUNBAR: That could also
24 be another --

1 MR. LEONARD: Typically, we
2 don't have too many employees missing that
3 deadline so they either choose one or the
4 other.

5 MR. SCOTT: So how is the
6 employee educated on the two different
7 plans?

8 MR. LEONARD: On their first
9 day of arrival, or first week of arrival, we
10 have employee orientation and our HR
11 Department provides as part of the
12 orientation two different plans and what is
13 expected from them and what the difference
14 is between the two plans.

15 MR. SCOTT: Does one plan
16 enable you to get a lump sum?

17 MR. LEONARD: Not that I'm
18 aware of, no. So when you say lump sum,
19 what do you specifically mean?

20 MR. SCOTT: I've heard of
21 DROP. I'm not sure what that is.

22 MR. LEONARD: No, we don't
23 have the DROP at PGW.

24 MR. SCOTT: What I was asking

1 is once one gets to the retirement age,
2 could they just say, Give me a million
3 dollars and I'm out of here?

4 MR. LEONARD: No.

5 MR. SCOTT: So they have to
6 take the benefits over time?

7 MR. LEONARD: They would have
8 to take the benefits according to whatever
9 the actuarial --

10 MR. DUNBAR: Someone in the
11 defined contribution, you could make a
12 larger withdrawal but you'll have
13 significant tax implications associated with
14 that, so a 401k plan like any other.

15 MR. LEONARD: From a 401, not
16 from PGW'S pension plan.

17 MR. JOHNSON: But I imagine
18 with the 401k, they can take their entire
19 balance and roll it over --

20 MS. RHYNHART: Right.

21 MR. JOHNSON: -- where this
22 plan does not offer that. We look at
23 retired participants. They went down
24 slightly as well. We had a higher number of

1 deaths in that group than we would've
2 expected to by our actuarial assumptions
3 this year. And terminated investments is
4 just a minor -- those are folks that have
5 left PGW but have not begun to collect their
6 pension as of these dates.

7 What we did see a pretty big
8 decline in was the total payroll from last
9 year to this year as well as average pay and
10 these two items contributed a lot to the
11 decline that we'll see on the next page in
12 the contribution levels for PGW.

13 Last year and the year before that
14 I believe, they went up fairly
15 significantly, those two numbers. So maybe
16 this year was sort of a balancing, you know.
17 I think last year was like 9% which is
18 quickly exceeding our 4.5% assumption. So
19 maybe that's something like a corrective
20 mechanism in place that got that back down
21 to more normal levels.

22 Any questions on that section?
23 That's a quick snapshot, again, fairly
24 consistent year over year of what we would

1 be expecting.

2 (No response).

3 MR. JOHNSON: Again, page 2,
4 just a quick overview. The contributions
5 this year have shown a decline. The primary
6 drivers of that decline were that decrease
7 in the cover of payroll in the average pay
8 that we saw on the prior page, more retiree
9 deaths than we assumed so we had an actual
10 gain from that.

11 In addition, there was an adoption
12 of an new mortality projection scale. We do
13 this every year. Each year they change a
14 little bit depending on the date that it's
15 fed into that projection scale.

16 And this year, the scale reflects
17 that people are actually living a little bit
18 less than we thought they were going to live
19 last year, so that brings our liabilities
20 down.

21 MS. RYHNHART: In your
22 mortality assumptions, do you assume going
23 forward that people will live longer?

24 MR. JOHNSON: Yes. So

1 gradually, they will live longer as we go
2 into the future. So it's not stacked. So
3 if somebody who is 65 today is expected to
4 live to 80. And in 20 years, somebody 65
5 might be expected to live to 82 or 83. So
6 that's how that sort of works.

7 MS. RHYNHART: Okay. So it's
8 very gradual?

9 MR. JOHNSON: It's
10 continuously gradual built in on extra
11 longevity. And that's built into our
12 mortality date and the liabilities of the
13 plan.

14 The net normal cost on the first
15 line there, it had a drop of about 6.2%.
16 The normal cost is just the value of the
17 benefits accrued by the employees in a
18 specific year. So if your plan -- if PGW's
19 plan was 100% funded, that would be the
20 annual cost of the plan.

21 So in this case, it would be about
22 7.3 million dollars. And that decline is
23 due to those drivers that I just cited there
24 that have worked positively this year. The

1 contribution dropped as well from last year
2 to this year.

3 PGW's funds, their past service
4 liability over an open 20-year-period were a
5 closed 30-year period. So as part of our
6 projections, the 20-year level is what
7 really controls for the first five or six
8 years. And after that, the 30 year will
9 overtake the 20 year and that will be a
10 larger payment. So that's what we're seeing
11 right now.

12 And then the percentage of payroll
13 has declined as well because the payroll
14 levels have declined and the contributions
15 have declined as well. One thing I'd like
16 to point out here is we've had this drop
17 from 28.7 to 26 points, so about a two
18 million dollar drop in the policy
19 contribution. We don't know what's going to
20 happen in the future.

21 My recommendation would be, and
22 this is just from an actuarial perspective
23 of somebody who looks to keep -- to get
24 plans fully funded, is to continue to fund

1 the plan at the higher rate, last year's
2 rate, let's say the roughly 29 million
3 dollars, rather than dropping down to the 26
4 million this year because we had these good
5 experiences here but that's no guarantee
6 that that's going to continue in the future.
7 So getting more money in the plan is really
8 in my mind good business practice.

9 And those higher contributions are
10 already built into PGW's rate structure so
11 the money is already there. So, again, this
12 is just a recommendation but certainly one
13 to discuss.

14 MS. RHYNHART: So the reason
15 that the -- just let me understand this.

16 MR. JOHNSON: Yes.

17 MS. RHYNHART: The reason
18 that it went down from 28.8 to 26.8, the two
19 million drop, was because of the mortality
20 change?

21 MR. JOHNSON: That was one
22 piece. The other was the decline of the
23 payroll. So we're assuming about a 4.5%
24 increase in payroll each year and it went

1 down.

2 MS. RHYNHART: So when you
3 smooth that or when you do the whole
4 calculation, you just ended up with a lower
5 --

6 MR. JOHNSON: Right. And
7 that reduction doesn't get all captured in
8 one year. It gets smoothed out over that 20
9 or 30-year period but it does bring the
10 contribution down two million dollars this
11 year. Now, that's not to say that next
12 year, the payroll goes up significantly
13 again and then we're back at a higher
14 contribution level.

15 MS. RHYNHART: Now, Dan, when
16 PGW gets approval, you have to get approval
17 from the PUC?

18 MR. LEONARD: That's correct.
19 So when we filed our last rates back in
20 2017, the proposal that we had submitted to
21 the PUC included the pension and the
22 contribution to be approximately 28 to 29
23 million dollars so that's already included
24 in our current rate structure.

1 MS. RHYNHART: And do you
2 think that -- I mean, I don't want to put
3 you on the spot with this. So it's already
4 included in the rates? Is it PGW's plan to
5 just continue funding it at that level?

6 MR. LEONARD: We typically
7 plan at the higher of the two, the 20-year
8 open amortization or the 30-year closed
9 amortization. However, we have -- I guess
10 since it's already embedded in the raise,
11 we're prepared to contribute up to the 28.8
12 million dollars if directed by the
13 commissioners -- or, excuse me, if directed
14 by the Finance Director.

15 MS. RHYNHART: Are you the
16 person that's the Finance Director's -- are
17 you Rob's sub?

18 MR. DUNBAR: Yes.

19 MS. RHYNHART: Okay.

20 MR. SCOTT: So that's the
21 Finance Director's decision and not PGW's?

22 MR. LEONARD: That's correct.
23 That's what happened a few years back with
24 paying the higher of the two, the higher of

1 the open -- 20 or open vs. the 30 or closed.
2 And if we are to contribute more than the
3 actual determined contribution, that would
4 be by the direction of the Finance Director.

5 MR. SCOTT: Why is total
6 payroll anticipated?

7 MR. LEONARD: I don't think
8 it was anticipated that full payroll -- it's
9 not necessarily total payroll for the entire
10 company. It's only those -- it's only
11 applicable periods. So applicable payroll
12 would be those employees that have been
13 elected to be part of the defined benefits.

14 So to the extent that we have older
15 employees that are leaving the company and
16 joining the new pension plan, that doesn't
17 include their salaries. And we have newer
18 employees that are making a lower wage.
19 Entering the defined benefit, that would
20 only be one factor that would contribute to
21 that decrease in payroll.

22 MR. JOHNSON: Any other
23 questions on that page there?

24 (No response).

1 MR. JOHNSON: And, again, I
2 don't want to step on anybody's toes with
3 the policies here. I just think that, you
4 know, we live in a world that's in highly
5 variable markets going up and down
6 unpredictably. And to have more money in
7 the plan will just give the plan more
8 cushion in the future as well as get towards
9 being fully funded at a quicker rate.

10 MR. DIFUSCO: Al, you might
11 get to this at a later page, and I've talked
12 a little bit about this with Joe Golding and
13 Dan. My understanding is that there's an
14 expected -- you're planning for a larger
15 number of retirements in the next 12 -- it
16 was I'll say 12 to 24 months. That was
17 going to be earlier and now it seems that's
18 been extended for a year or so.

19 Like have you preliminarily, Al,
20 looked at that? Is that one of the reasons
21 you're recommending to keep the 28.8 that
22 you're anticipating as kind of like, you
23 know, a small spike in retirements?

24 MR. JOHNSON: That's one part

1 of it. I mean, you know, just the general
2 business practice is to just trying to get
3 more -- get additional funds in there. But
4 if we do have a spout of retirements, that
5 generally will increase liability and then
6 it's going to increase cost. So if we're
7 going to anticipate -- you know, I think the
8 union -- is the union contract coming up
9 soon?

10 MR. LEONARD: The union
11 contract is set to expire -- will be renewed
12 this May, May of 2020. So typically around
13 the contract time, either the December
14 before or the December after, we see a surge
15 in the amount of retirees for one reason or
16 another.

17 So we're anticipating that either
18 this December we're going to have an
19 increase compared to what trends typically
20 are or next December compared to what trends
21 typically are. It depends on, I guess, the
22 outcome of the contract.

23 Some people are fearful that the
24 contract would change. Therefore, we have a

1 surge in retirees the December before. And
2 some people don't like the terms and
3 conditions of the new contract so we have a
4 surge of employees that are retiring after
5 the contract.

6 MR. DIFUSCO: Okay. Thank
7 you.

8 MR. JOHNSON: I'm going to
9 turn over to page 3 if there's no more
10 questions. Again, just stop at any point
11 with questions.

12 So this year, what we call the
13 unfunded accrued liability dropped about 7%,
14 so going in the right direction. Again, all
15 the factors that I cited about lower cover
16 payroll and, you know, having more favorable
17 experience on our actuarial assumptions.

18 So it's the 206 million is all
19 liabilities of roughly 756 million so the
20 plan is about 73% funded as of July 1, 2019.
21 So we have about \$0.73 saved for every
22 dollar of future benefits that we owe. So
23 we have to make up that gap either through
24 investment returns or employer

1 contributions.

2 Turning to page 4, we showed the
3 market value and actuarial value of assets.

4 A number of years ago, PGW implemented an
5 actuarial value of assets to determine their
6 contributions. What essentially that does
7 is that smoothes market values over a
8 five-year period. So you phase in 20% of
9 the loss each year into the actuarial value
10 of assets.

11 And over the period of the market
12 value ups and downs, they all average out,
13 keeping an asset value that's relatively
14 smoother than a market value and making
15 contributions more level as well. So that
16 was a prudent step just to be able to make
17 contributions, annual changes more
18 predictable and not be subject to all 100%
19 force of any market swings year over year.

20 And there is a 20% constraint so an
21 actuarial value of asset cannot be greater
22 than 120% or less than 80% of the market
23 value so it keeps it somewhat in the
24 neighborhood.

1 I just want to jump to page 12. A
2 lot of those intervening pages are a lot of
3 actuarial calculations. I don't know if
4 anybody would be -- if anybody's interested
5 in them, let me know but that's kind of the
6 boring stuff.

7 We can jump over to page 12. Here
8 is an estimated ten-year projection of the
9 benefit payouts from the pension plan. And
10 we can see it's based on the current age and
11 service of the group and the size of their
12 salaries and it's going to just gradually
13 increase over time. This is assuming that
14 all of our actuarial assumptions are met
15 exactly in the future which we know that
16 won't happen.

17 But for the purposes of these, you
18 know, trends, that's how we do the
19 calculations. So just gradually increasing
20 about ten million dollars over the ten-year
21 period.

22 MR. DIFUSCO: So, Al, the way
23 to think about this is that about half the
24 money every year -- at least based on the

1 current payment schedule, about half the
2 money is coming out of the fund itself to
3 pay for benefits and then the other half
4 roughly is coming, I mean, give or take,
5 that the other half is coming from PGW's
6 contributions?

7 MR. JOHNSON: Correct.

8 MR. DIFUSCO: 'Cause I'm used
9 to, you know, paying -- and I update the
10 commissioners every month but it's similar
11 to, I would say, 2 or 2.5 million, sometimes
12 a little lower, sometimes a little higher
13 that were drawn from the funds --

14 MR. JOHNSON: Right.

15 MR. DIFUSCO: -- with the
16 rest being paid by PGW?

17 MR. JOHNSON: Correct.

18 MS. RYHNHART: And then the
19 employee contribution is a very small piece
20 of that?

21 MR. DIFUSCO: A small piece
22 of that. That comes in every so often and
23 is immediately swept over into the cash
24 account and then if prudent, reinvested. It

1 comes in like monthly or every two to four
2 weeks, something like that.

3 MR. JOHNSON: So the employee
4 contribution is about 1.5% paid out but
5 they're expected to rise to 6 --

6 MS. RHYNHART: Expected like
7 it's already in the contract?

8 MR. JOHNSON: Yes. 'Cause
9 all new employees have to pay that 6%
10 employee contribution to be in the defined
11 benefit plan. Employees I think before -- I
12 can't remember exactly if it was 2011, they
13 didn't have any employee contributions
14 required in the plan.

15 MS. RHYNHART: Right.

16 MR. JOHNSON: All right. We
17 can turn over to page 13. Here is a
18 historical look back over the last eight
19 years of PGW's funding progress and what's
20 occurred along the way. So as you can see,
21 we've had generally an increase in the
22 funding levels.

23 And there's been a couple times
24 where it was -- the investment return

1 assumption was dropped based on market
2 conditions and things of that nature. So we
3 had some choppy waters there in 2015 and '16
4 where we lost some ground as we changed
5 those assumptions to be more conservative.

6 But then since then, as the funding
7 mechanism works, we're starting to build
8 back up again so we're moving the plan
9 slowly towards being fully funded. That's a
10 bit down the road but that's how the method
11 works here. So that gives you an idea of
12 where you've been.

13 And if you flip over to page 16,
14 here is a projection of where the plan is
15 going. Again, this is a ten-year forward
16 looking cash contribution forecast and how
17 we can expect funding status to evolve over
18 time. Again, this is assuming that all of
19 our assumptions are met exactly in the
20 future which we know won't happen.

21 But if they are, you can see a very
22 gradual increase in the funding status of
23 the plan from 72 to 78 over that ten-year
24 period. And that's really due -- it is

1 gradual because of the nature of how we're
2 funding the past service liability over 20
3 and 30 years.

4 So it's going to take that amount
5 of time to get to a fully-funded position
6 but if our substances work out the way we
7 think they will versus how we project the
8 assets, the liabilities, and then the
9 funding status of the plan to go.

10 MR. DIFUSCO: Now, this is
11 assuming the 26.8, and if the Finance
12 Director and PGW were to accept your
13 recommendation to do 28, these numbers would
14 move up most likely?

15 MR. JOHNSON: They would all
16 move up.

17 MR. DIFUSCO: Do you have any
18 idea how much?

19 MR. JOHNSON: I would say
20 about half a point.

21 MR. DIFUSCO: Each one would
22 move up half a point or would it add on?
23 Each one individually or would it --

24 MR. JOHNSON: I would say

1 each one individually.

2 MR. DIFUSCO: Okay. So we'd
3 go to like 73.1 just hypothetically if we
4 brought in --

5 MR. JOHNSON: Correct. And
6 the end there, that may come up a little bit
7 more, maybe more towards the 80 if that was
8 done. I mean, that's something that we can
9 run out fairly simply and update and refresh
10 the exhibits.

11 MR. DIFUSCO: That might be a
12 good idea.

13 MR. DUNBAR: That's assuming
14 the rate stays the same at 7.3?

15 MR. JOHNSON: Right. And in
16 real life, we know there's going to be ups
17 and downs. We saw it on the historical
18 chart previously. You're never going to get
19 that sort of steady increase. There's going
20 to be bumps in the road along the way. But
21 the way the funding method works is that you
22 get those and eventually it gets back on
23 track again to start moving towards 100%.

24 MR. SCOTT: So you projected

1 that we would be this year at X. Are we in
2 compliance with your projections, slightly
3 over, slightly under?

4 MR. JOHNSON: I think we were
5 slightly over. So we did better because we
6 had better experience than we anticipated.
7 So we were probably about -- I think we
8 estimated we were recommending 71.5% funded
9 and we came in at at 72.6. So we did a
10 little bit better this year due to those
11 factors.

12 MS. RHYNHART: The
13 information on page 12, is this provided
14 anywhere where it shows the ten years going
15 forward, the amount coming out of the plan?
16 What Chris was saying, the amount coming out
17 of the plan, projections to come out of the
18 plan, the amount coming from PGW, and the
19 amount coming from the employees so we can
20 see how much is actually coming out of the
21 plan, what the trends --

22 MR. JOHNSON: We can
23 superimpose that. We could add columns to
24 this if that's something that you want to

1 see.

2 MS. RHYNHART: Okay. That
3 would be helpful, yes. I would like to see
4 that.

5 MR. JOHNSON: So you would
6 like to see, just to clarify that, what PGW
7 is expected to put into the plan?

8 MS. RHYNHART: Well, so out
9 of this 56 million, that's coming from
10 somewhere, right? That, you know, 26 to 28
11 million is coming from PGW, X amount is
12 coming from employees, and X amount is
13 coming from the plan itself.

14 MR. JOHNSON: Got it. Okay.

15 MS. RHYNHART: Okay, great.

16 MR. SCOTT: Did you say it
17 was like 50/50?

18 MR. DIFUSCO: Excluding the
19 employee contributions. I'm just putting
20 those aside for the moment. I get that it
21 would rise to 6. But, yes, I mean, on an
22 average month and when you get the e-mails,
23 you see somewhere between 1.9 and 2.5
24 million being gone out of the account, give

1 or take.

2 So just quick math, right, times --
3 I mean, it's 45 to 55%, give or take. And
4 then as Rebecca said, if we could get three
5 columns that could break it down, you know,
6 to be more precise? I would estimate it's
7 about that.

8 MS. RHYNHART: PGW's
9 contribution is actually showing a projected
10 decline that's why I was asking.

11 MR. JOHNSON: In the
12 projections?

13 MS. RHYNHART: Yes. So
14 that's why if this -- if the expected payout
15 is going up and then -- like I'm --

16 MR. JOHNSON: Right. The
17 contribution is going down as part -- as the
18 plan gets closer and closer to being fully
19 funded, that contribution is going to
20 continue to come down because there's no
21 need.

22 Basically, what we're saying is the
23 past service liability is going to be paid
24 off so then all that will really be -- once

1 the plan is 100% funded, really all you'll
2 need to put in annually is what's called the
3 horse --

4 MS. RHYNHART: The horse,
5 right.

6 MR. JOHNSON: -- which is
7 down to about 7 million. So, eventually, if
8 we kept running this out, we'd get down to
9 about -- it wouldn't be 7 'cause its normal
10 cost is going to grow every year, but you
11 would get down a level that might be more
12 like ten million dollars.

13 MS. RHYNHART: So going back
14 to page 12, there's more and more due to
15 retirees. So the assumption is that the
16 investment returns at 7.3% are going to pay?

17 MR. JOHNSON: That's right.
18 What makes it up is the employer and
19 employee money plus the investment return.
20 That's one side of the equation. The other
21 side is benefit payments and expenses that
22 come out of the plan. Those two over the
23 course of a plan's lifetime have to be equal
24 to each other. It's just a matter of how we

1 slice and dice it over the evolution of the
2 plan.

3 The next two pages, I don't -- this
4 is just showing what the contributions would
5 be if we were just on the 20-year policy
6 versus the overlay of the 30 year. And then
7 the page after that is if we were just on
8 the 30-year policy so just supplementary
9 schedules. But really, the funding policy
10 of the plan is on page 16 where we're
11 showing that.

12 If we turn to page 19, the rest of
13 the pages in here are really just some
14 additional demographic breakdowns for the
15 active participants, the retirees, and the
16 terminated benefit folks. So it's just a
17 way of giving you, you know, how folks are
18 sitting.

19 If we turn to page 20, the active
20 employees, there's service buckets on the
21 top row and then their age is down the side.
22 So there are -- at July 1, 2019, just to
23 give you some idea, 16% of the population
24 here is eligible for unreduced pension so

1 those are the people that have exceeded 30
2 years of service, and an additional 5% are
3 eligible for retirement.

4 So you have one out of every five
5 employees here is eligible to retire. So
6 that could be -- you know, if you had an
7 outflow of people in a retirement situation,
8 that could have a disruptive effect on the
9 plan as well as just the operations of the
10 organization itself. You're losing a lot of
11 steam, your people with a lot of knowledge
12 to retirement, that could have an impact on
13 PGW itself, its internal operations.

14 And then just if we turn to page
15 22, here is a data reconciliation. So on
16 the first page, I showed the snapshot at
17 7/1/18 and 7/1/19 and this is how we got
18 from point A to point B. So it's the ins
19 and outs in those particular -- in three
20 different classes that we look at; actives,
21 terminated investments, and retirees.

22 And then the last section is our
23 actuarial assumptions and methods kind of
24 lined out for you. The mortality table that

1 we use is an industry table. It's published
2 by the Society of Actuaries and it's based
3 on current mortality for private sector
4 plans so you're really using your most
5 up-to-date mortality table here.

6 All the other assumptions are PGW
7 specific so they're based on the experience
8 of PGW employees. It's been about five
9 years since we did an actuarial study of the
10 assumptions and I'm going to recommend at
11 the end of this year that we perform a
12 comprehensive analysis of all of the PGW
13 actuarial assumptions, confirm if we're --
14 validate whether our assumptions are still
15 good or if we need to update our
16 assumptions. So that would be the next item
17 that I would propose that we do.

18 And any changes that I would
19 recommend would first take effect for the
20 July 1, 2020 evaluation. So this evaluation
21 is complete which means it would be in the
22 subsequent evaluation, we would be making
23 the adjustments to assumptions.

24 MS. RYHNHART: Chris, how

1 often do we redo the experience to date for
2 the City's main pension plan?

3 MR. DIFUSCO: I want to say
4 every three years.

5 MS. RHYNHART: Every three?
6 Right, that's what I thought. Five years is
7 a long time.

8 MR. JOHNSON: Yes, I mean,
9 the standard is -- generally, three to five
10 years is sort of the range where five is
11 starting to push the edge. Three is -- and
12 if you have a lot of change going on, things
13 are -- I would recommend doing it more
14 frequently just, you know, to keep your eye
15 on things.

16 But this plan I think is fairly
17 uniform. We've had experience over the last
18 five years that's been very close to what
19 our assumptions are showing is correct.
20 That's not to say each individual assumption
21 is correct. That just says that in the
22 aggregate, we're close to where we think we
23 would be.

24 And that's why we haven't really --

1 probably don't want earlier but at the
2 five-year mark, it's certainly time to do
3 one itself. We'll put that on our to-do
4 list for -- I think Q4 is when we'll get it
5 done and then we'll review with you folks
6 about the assumptions and the impact on cost
7 and contributions.

8 MR. DIFUSCO: And there's
9 certainly nothing, once you do it this year,
10 to prevent PGW or the commissioners from
11 saying three years from now or four years
12 from now.

13 MR. JOHNSON: No, not at all.

14 MR. DIFUSCO: Certainly, I
15 would agree. I mean, you talked about doing
16 it this year. There's nothing from stopping
17 us from doing it frequently.

18 MS. RHYNHART: Do we need to
19 vote on that -- vote on doing it?

20 MR. JOHNSON: I wouldn't
21 think so. This is something as part of my
22 -- the stance and practice that I have to do
23 this at some point.

24 MS. RHYNHART: Okay.

1 MR. JOHNSON: I mean, if you
2 choose to vote on it, that's fine, but I
3 don't think we need to.

4 And then the final section there is
5 a summary of the plan provisions. So these
6 are high-level summaries of benefits that
7 employees of PGW are going for. Any more
8 detail on that would be found on the plan
9 documents.

10 I think that's about it from my
11 perspective. Are there any other questions?
12 I've got a couple takeaways.

13 MS. RHYNHART: I do have a
14 question. I mean, this isn't in this
15 presentation. It's in this book, the cash
16 flow, which is right behind this green --

17 MR. JOHNSON: I brought
18 copies of it with us. This is the 20-year
19 projections that we had done.

20 MS. RHYNHART: This is just
21 the cash flow. Well, it's ten years; 2018
22 to 2028. Do you have copies?

23 MR. JOHNSON: I don't have
24 copies for everybody. We just made copies

1 so we have some available.

2 MS. RHYNHART: That's okay.

3 So the cash flow of this plan is really
4 negative.

5 MR. JOHNSON: Yes.

6 MS. RHYNHART: So it goes
7 from -- 2018, it goes from negative 4.7% and
8 goes up to negative 6. I mean, this -- I
9 wanted to just have a conversation around if
10 there's a concern around that because -- and
11 maybe there's not. Maybe there shouldn't
12 be.

13 MR. JOHNSON: Are you looking
14 at the one that says 7.3% annual investment
15 --

16 MS. RHYNHART: Yes.

17 MR. JOHNSON: And there was
18 one that also was 0%.

19 MS. RHYNHART: Yeah, I'm just
20 looking at -- so, for example, on the City's
21 main -- the City's pension plan, the big
22 pension plan for fire, police, DC-33, and
23 white collar and blue collar workers, we
24 have a positive cash flow which comes from

1 also -- I mean, the plan's very different.
2 It's only 45% funded. It's a very different
3 beast, right?

4 MR. DIFUSCO: That's a good
5 word.

6 MS. RHYNHART: Yeah. So
7 normally, I mean, you don't see negative
8 cash flow below -- I mean, my understanding
9 is also, oh, you want to see cash flow at
10 negative 3% or better. That was what I've
11 always -- you know, so you want to see that.

12 You don't want to see negative 4,
13 5, 6%. I don't know. I'm sure you do this
14 for other places and other pension plans so
15 I was wondering what you thought about if
16 this is a concern.

17 MR. JOHNSON: Well, as I was
18 mentioning earlier, I think, you know,
19 higher employer contributions are better for
20 funding a plan. You're going to -- what
21 happens is as you see these going down,
22 you're going to -- the plan will rely a bit
23 more on investment income to make up, you
24 know, for those gaps.

1 When you have a 0% rate of return,
2 you can -- I think you have that one there
3 as well, the net cash outflow is less than
4 it is under the 7.3 because you're not
5 getting any investment income so more
6 employer money is coming into that plan. So
7 it's going to offset that.

8 MS. RHYNHART: The PGW
9 contribution goes to 47 million in that
10 situation which I don't know what type of
11 raise that would need.

12 MR. JOHNSON: And that's
13 assuming that we're not earning any
14 investment income going forward.

15 MS. RHYNHART: I just want to
16 make sure we're all looking at it together
17 because if there is -- because of the
18 negative cash flow, if we don't hit a 7.3%
19 return, that is going to go fly right to PGW
20 to get -- to need an increase in rates. And
21 so, I mean, there's -- I don't know.

22 Maybe you already talk about that
23 and build that in to like what -- like okay,
24 if you get a shock, if something like '08

1 happens again, you know, for one year, if we
2 lose 30%, what do we need to go to the PUC
3 for? And maybe you're already talking about
4 that but I just want to make sure everyone's
5 thinking about it to put it together.

6 MR. JOHNSON: So in this
7 plan, you're relying more on investment
8 income to make up the gap. So if you're
9 balanced out, you're not as worried about
10 ups and downs in the market because the
11 money you have coming in is equal to the
12 money you have going out. You're not
13 relying on investment returns to meet any
14 gaps because there aren't any gaps.

15 So that's just the -- that is going
16 to be the nature of this, is that we're
17 relying on that. So then if that net cash
18 flow goes to negative 10 or negative 15,
19 you're going to have normal reliance on that
20 investment return. And if you have a bad
21 year, it's going to be more and more of a
22 shock to the system going forward.

23 It's why I always promote higher
24 employer contributions to the plans and

1 that's just my actuarial nature. My
2 character is that, you know, I don't want --
3 it's a great investment income and these
4 guys do a great job of it. But as we know,
5 when the markets crash, it's not -- there's
6 nothing Marc can do about when, you know, we
7 have a complete meltdown.

8 But having a structure in place
9 that's saying that, you know, the money
10 coming in is equal to the money going out,
11 we get that -- we're going to get that money
12 back slowly but it's not going to affect our
13 rates or affect contributions as much going
14 forward. But that would take a, you know,
15 decision to say maybe we want to fund this
16 plan at 40 million a year. Now, that has to
17 go into rates and --

18 MS. RYHNHART: Well, that's
19 --

20 MR. JOHNSON: I know. But
21 what I'm just saying is, you know, any extra
22 dollars that go into the plan, that makes it
23 more well-funded, it makes it a safer plan,
24 and more able to withstand downturns and not

1 have very, very poor outcomes if those
2 downturns do come falling down.

3 MR. CAWLEY: Excuse me. Can
4 I interject for a second? I think it's a
5 question -- I'm Robert Cawley. I represent
6 the retirees, both union and non-union. I
7 think if we would lower our discount rate
8 lower than 7.3, that would give us a
9 cushion. We haven't had a serious
10 correction in a few years.

11 I don't think your actuary form --
12 I didn't see anything where you have like
13 one down here or over the next ten. You're
14 assuming we go up to 7.8 in the next. We
15 didn't do it in the last ten. We're exactly
16 where we were. I think -- you're saying
17 bring more money in from the employer at I
18 think a lower discount rate. So 7.3 is a
19 little higher than the national average.

20 MR. JOHNSON: That's
21 certainly another option.

22 MR. CAWLEY: 6.8 would be
23 fair. The company -- I think they're going
24 to have to have more money but that would be

1 a cushion to talk about.

2 MS. RHYNHART: Well, I think
3 there should be a discussion around having a
4 plan to lower it. I mean, that's -- you
5 know. 7.3 is on the higher end of what's
6 assumed.

7 MR. LEONARD: Can we go off
8 the record?

9 MS. RHYNHART: I don't know.
10 Are we allowed to?

11 MR. LEONARD: I don't know.
12 I'm asking.

13 MR. DIFUSCO: Not with a
14 quorum.

15 MR. LEONARD: Oh, okay.
16 Never mind then.

17 MS. RHYNHART: I mean, we can
18 continue the conversation next time. We can
19 continue it next time. Do you want to just
20 continue?

21 MR. LEONARD: Yeah.

22 MS. RHYNHART: Okay.

23 MR. JOHNSON: I think it's a
24 good concern to raise though. I do

1 absolutely.

2 MR. SCOTT: Any other
3 questions?

4 (No response).

5 MR. SCOTT: Do we have to
6 take a form of action to accept this report?

7 MR. DIFUSCO: No. But when
8 the revised copy, you know, comes back with
9 the additions that your team is going to
10 add, I'll distribute it to the commissioners
11 electronically.

12 Assuming there's no further
13 questions or requests for modifications or
14 edits, then, you know, we can take the draft
15 off after they've had a chance to look at
16 it. And at that point, it would become --

17 MR. JOHNSON: And I'll get
18 our signatures in there as well.

19 MR. DIFUSCO: Yeah. And once
20 we know there's no further needs --

21 MR. JOHNSON: So we need
22 another draft with the updates?

23 MR. DIFUSCO: Yeah. And then
24 once we see that that's okay, then we'll

1 say, okay, go ahead and take the draft off
2 and sign it.

3 MR. JOHNSON: And we'll sign
4 it. Okay.

5 MR. DIFUSCO: And we'll
6 publish it on the website for everyone when
7 it's done.

8 MR. JOHNSON: Perfect.

9 MR. DIFUSCO: Thank you.

10 MR. SCOTT: So there's an
11 assumption that PGW's contributions going
12 forward will remain the same? That's an
13 assumption?

14 MR. LEONARD: I don't know.
15 I'm not quite sure I understand what you
16 mean by assumption. I think we're willing,
17 with the direction of the Finance Director,
18 to contribute up to the 28.9 million
19 dollars. So we're willing to do that. We
20 have the ability because it's already in our
21 ways to do that.

22 MR. SCOTT: So you're saying
23 it's a given?

24 MR. LEONARD: I'm not saying

1 it's a given. I'm saying we have to be
2 directed. Currently, we're directed to
3 contribute to the higher of the two. So to
4 the extent that this is even more than the
5 higher of the two, the 30 year closed or the
6 20 year open, we would need direction from
7 the Finance Director.

8 MS. RHYNHART: They could use
9 that two million for something else if we
10 don't direct -- if the Finance --

11 MR. LEONARD: That's correct.

12 MS. RHYNHART: -- Director
13 doesn't direct them, which isn't -- I would
14 say that the rate payers are under the
15 impression that they're paying for their
16 pension with that. But anyway, the Finance
17 Director needs to direct them.

18 MR. LEONARD: That's correct.

19 MR. DIFUSCO: So, Don,
20 annually, the Finance Director will look at
21 all the assumptions in the plan, the
22 payments, the assumed rate of return, and
23 then he gives instruction to PGW/the
24 actuary/the commission. Like here are the

1 changes that we're going to make this year
2 or not.

3 And so if we were to change any of
4 the assumptions, the assumed rate of return
5 and the 28.9, he needs to send a letter
6 basically determining those changes. It's
7 not like the munie fund where the
8 non-trustees around the table set the rate
9 or set the assumptions. In this case, the
10 legislation invests that according to the
11 Finance Director.

12 MR. SCOTT: Okay.

13 MS. RHYNHART: I think that
14 opinion was sent to me like day one on the
15 job.

16 MR. DIFUSCO: Probably. I
17 think you had a lot of stuff that day. I
18 don't think that was the only thing they
19 sent.

20 MR. WHITE: It was day five.

21 MR. DIFUSCO: In fairness, it
22 was not a big pile of stuff.

23 MR. SCOTT: Okay. Thank you.

24 MS. RHYNHART: Are we doing

1 this -- the agenda?

2 MR. DIFUSCO: The asset
3 allocation? I was actually just going to
4 say --

5 MS. RHYNHART: I'm sorry.

6 MR. DIFUSCO: No, it's fine.
7 So I had suggested, and I think I got some
8 feedback from folks, that deferring the
9 discussion on asset allocation, the proposed
10 allocation alternatives in light of all the
11 information we've considered today, the
12 revisions that are coming from Al and his
13 team that we would defer discussion and to
14 vote on agenda item -- I guess it's four
15 until November 13th. So we're going to
16 remove that on the agenda and just move to
17 investment performance.

18 MR. SCOTT: I wanted to ask
19 one question.

20 MR. DIFUSCO: Sure.

21 MR. SCOTT: Rebecca, this
22 discussion took place before you came.

23 MS. RHYNHART: Okay.

24 MR. SCOTT: And what we were

1 -- the question I asked was is there a
2 requirement that we actually have an
3 actuarial study? And Chris told me that
4 from the City, yes, there is. But for PGW,
5 there isn't.

6 MR. DIFUSCO: I said I
7 haven't reviewed the legislation. I haven't
8 had my counsel to the commission hat on many
9 years. So I asked Adam and Ellen to check
10 whether or not it's in the -- he's going to
11 -- the law department is going to see what
12 the legislation says and we'll pass that
13 along.

14 I know in the Code there's specific
15 reference to the -- it's either every year
16 or every other year. I recall that. The
17 PGW legislation I haven't looked at in a
18 while.

19 MS. RHYNHART: Yeah, take a
20 look at it and see.

21 MR. DIFUSCO: But Adam and
22 Ellen will send something over.

23 MR. SCOTT: Okay. Thank you.

24 MR. DIFUSCO: But, yeah, we

1 have moved to something where we do it every
2 year. As you know, that was not always the
3 case in years past. But we'll get that
4 opinion after.

5 MR. DUNBAR: So are we
6 skipping on the asset allocation discussion
7 because we thought it would be too much in
8 conjunction with the report?

9 MR. DIFUSCO: Yes. And also
10 because if there's going to be discussion
11 about increased contribution levels and a
12 discussion offline with the Finance Director
13 about a lower superior return in the future,
14 that would impact, right? I mean, that
15 changes all the scenarios, right?

16 Suddenly, if you go to 7.2 or 7.1
17 or 7.15, that has a material impact on what
18 PFM and staff may recommend. So the idea
19 was let them present their revised report,
20 have the conversations with the Finance
21 Director, see if the increased contributions
22 are going to come in, and come back on the
23 13th with all of that like new and refreshed
24 information and discuss it then.

1 MR. DUNBAR: Okay.

2 MR. DIFUSCO: Is that --

3 MR. DUNBAR: Yeah, that's
4 fair. I thought it was more of a discussion
5 about the idea of alternatives and I'm sure
6 over time, you know, those will get tweaked
7 because this is going to always be an
8 ongoing moving sort of -- moving target
9 depending on what's happening in the market,
10 depending on what's happening from a
11 contribution perspective.

12 But I thought this was more of a
13 discussion about the idea of moving towards
14 alternative period and then we will always
15 be making those adjustments, but we can
16 certainly move it 'til November.

17 MR. DIFUSCO: Okay.

18 MR. SCOTT: All right. Well,
19 the next item on the agenda is investment
20 performance review.

21 MR. GOLDSMITH: Sure. Before
22 I get into that, I want to say, you know, if
23 there are questions related to the asset
24 allocation related to adjusting the

1 investment policy, you know, our views on
2 what was discussed today, you could reach
3 out on the next several months.

4 The last tab of the books includes
5 flash performance for the month of July as
6 well as the month of August. September has
7 just ended so we don't have really a true
8 indication of performance. We have a modern
9 indication.

10 You know, very briefly, the first
11 report here is for July. It was a good
12 month of the plan; up 0.6%, outperforming
13 its benchmark net of fees.

14 MS. RHYNHART: Where are we?

15 MR. GOLDSMITH: The very last
16 tab. I'm sorry. The very last section of
17 it.

18 MS. RHYNHART: I missed it,
19 where the investment guidelines are changed
20 here. Are we going to talk about that?

21 MR. DIFUSCO: That's part of
22 the -- if you move to alternatives.

23 MS. RHYNHART: Oh, okay.

24 Good.

1 MR. DIFUSCO: No, we're not
2 changing anything. That's based on the
3 current -- nothing is changing.

4 MS. RHYNHART: Okay. Thank
5 you.

6 MR. GOLDSMITH: So, again,
7 very briefly for July, you know, July was a
8 good month for equities and stocks, U.S.
9 stocks in particular. So that was largely
10 responsible for the plan's outperformance.
11 You get 0.63 versus 0.5 net of fees.

12 Additionally, very briefly on page
13 2 for the July report, there were some
14 strong contributions from the credit and
15 high-yield managers; Logan's Circle,
16 Investment Grade Credit, and Sky Harbor
17 pretty significantly outperforming the
18 current place aggregate in the month of
19 July.

20 Flipping ahead now through the
21 green page, the provider page, now we're on
22 to the Philadelphia Gas Works Pension Plan
23 monthly performance review, month ended
24 August 31st.

1 And then so August was a bit of a
2 different overpersonal of the trend that
3 we've seen most of this year with few
4 exceptions. It was a negative month for
5 equities if you just think back to where we
6 started the end of July. We ended that
7 month with the first cut to the Fed rates in
8 ten years and an erosion of, you know, or I
9 can say stepping back from the table of U.S.
10 and China relating to trade discussions. So
11 that's in equities.

12 You can see, you know, U.S. stocks
13 were down 1 to 2% for the month of August.
14 The plan as a whole was down for August,
15 down 1.09% net of fees versus the benchmark
16 which was down 0.63% net of fees. On a
17 year-to-date basis, moving out several
18 columns to the right, the plan is up 13.05%,
19 so a very strong absolute return year to
20 date. You know, adding to the experience I
21 guess if you're looking at it from an
22 actuarial basis. A slight lag in net of all
23 fees relative to the benchmark 13.2, so
24 13.05 to 13.2 year to date.

1 Asset allocation, the overweight to
2 equities, has been a net contributor to the
3 plan while there has been some detractors on
4 the active side as well as the overweight to
5 small caps through August has been a
6 detractor. And the fixed income component
7 of the plan has an overweight to the
8 intermediate fixed -- duration fixed income
9 which more recently. You know, as fixed
10 income markets become more volatile, that
11 has been a detractor.

12 You know, so I'll just go back to
13 the top. And moving through the individual
14 sectors that, you know, combine large cap,
15 you know, just behind the benchmark minus
16 the 2.07 versus minus 1.83, most of that
17 relied on PineBridge. They lagged for the
18 quarter. They lagged by approaching 400
19 basis points year to date. That was a fund
20 that was added at the end to being in 2018,
21 2017.

22 You know, we had a call with staff
23 in PineBridge last quarter. You know, we're
24 expecting their quarter-end information to

1 arrive today and at which point make a
2 determination whether they, you know, need
3 to go on watch list or not. As of their
4 August report, much of the underperformance
5 year to date, really all of it was
6 contributable to stock selection not sector
7 allocation and really within one of their
8 factors that they refer to as mature
9 defensive.

10 So a lot of their selection within
11 the mature defensive realm has been a
12 detractor this year. You know, that's not
13 entirely alarming given that, you know,
14 their benchmark is up 18.3%. So, you know,
15 while we do want to get a handle on why
16 their defensive positioning is what's
17 bringing them down in a sharply up market,
18 that's less of a red flag than it would be
19 if the market was eroding.

20 MR. DIFUSCO: Can we spend
21 just another -- we did have that call and I
22 know there was a lot of, you know, I think
23 vigorous debate and discussion when we got
24 rid of some of the other active managers.

1 These were obviously -- these folks were
2 hired as low fee. I think they even
3 described themselves maybe reluctantly as
4 the enhanced index, right, when we hired
5 them. And they do have a very low fee.

6 But, you know, I know we talked
7 about -- look, they're in a really --
8 they're probably the most efficient space in
9 the entire market, right? So if they were
10 trailing index slightly -- I'm just curious
11 to see what, you know, your research team
12 and what you folks decide in terms of watch
13 or where they're at because, you know, I'm
14 not in favor of necessarily terminating
15 managers too quickly.

16 But at the same time, the level --
17 and you know this 'cause we've talked about
18 it offline, the level of underperformance
19 given kind of what they're required to do,
20 it is a little concerning. I'm sure the
21 commissioners are on board and it is to me.

22 MR. GOLDSMITH: You're
23 correct. We sort of classify that as their
24 enhanced index. They do reluctantly like

1 to, you know, say that. You know, they try
2 to remain sector neutral when it comes to
3 their portfolio positioning so no big
4 overweights to consumer financials, et
5 cetera. You know, I would say that their
6 tracking error relative to the index has
7 been a little higher than expected this
8 year. And, again, that's been mostly
9 attributable to individual selections.

10 So, just as an example, and this is
11 over the last three months ending August,
12 you know, one of their big contributors was
13 an underweight to Philip Morris. At the
14 same time, one of their big detractors was
15 overweight to Altria Group. And so that is
16 an example of, you know, the sector
17 positioning hasn't changed.

18 They're in the consumer --
19 specifically cigarettes but their model is
20 directing them to overweight one player
21 relative to another. And, you know, the
22 benefit in underweighting Philip Morris was
23 offset from the overweight of Altria. So
24 that's an example of, you know, what is

1 their model in directing within that one
2 sector? So things like that have
3 contributed to a higher tracking error this
4 year.

5 And that's also I think maybe why
6 they would sort of reluctantly call
7 themselves an enhanced index. They will
8 make bets between two companies like that.
9 And so, again, we want to understand, you
10 know, why this year their selection is off
11 relative to prior years.

12 MR. SCOTT: What does the
13 watch list mean?

14 MR. AMMATURO: A watch list
15 means a manager that comes under closer
16 scrutiny. The watch list means they're all
17 on a track. If performance doesn't improve
18 on an absolute or relative basis,
19 termination's in the cards. So that's one
20 step closer to termination and more
21 scrutiny.

22 MS. RYHNHART: What's the
23 downside by putting them on watch list?

24 MR. AMMATURO: I think we

1 want to hear the commentary that they have
2 'cause the quarter just ended, Rebecca. So
3 we just want them to come to us with
4 commentary, deep attribution analysis. Once
5 we look at that analysis, we can make a
6 conclusion whether or not watch list is
7 warranted the next time we're together in
8 November. The quarter just ended yesterday
9 so we just want that time to do an analysis
10 on the attributions.

11 MS. RHYNHART: So you're
12 going to come next month? You would like to
13 come next month -- to come back and say,
14 Wow, it's doing --

15 MR. GOLDSMITH: We make our
16 -- we have one defined ranking system and we
17 make those decisions on a quarterly basis.
18 You know, like Marc said, it just ended. So
19 by the time the next meeting reaches, we
20 would've already reached that decision and
21 we'll be -- you know, we'll notify you as to
22 where PineBridge is ranked at that time.

23 But that decision will be made at
24 some point, you know, again, over the next

1 three or four weeks as we -- as the
2 information from the manager rolls in and we
3 are actually able to speak with them
4 following the end of the quarter.

5 MR. AMMATURO: And to Alex's
6 point, if the models tell them to select
7 high-quality stocks, that has not been the
8 place to be. When the market's up 18%,
9 high-quality stocks usually don't keep up in
10 a month that's up 18%. So that's probably
11 very telling if that's what the models say.
12 We'll take a deeper dive, obviously.

13 MR. GOLDSMITH: And, again,
14 at the same time, you know, they did
15 underperform just for the one-month period.
16 You know, the stocks were off this month.
17 So that's why we want to, you know,
18 basically create a designation. It's not so
19 much for us but also for you, to remind you
20 that this is where we stand here.

21 I mentioned small caps. You know,
22 for the month, you can see the combined
23 small cap. Active management, particularly,
24 you know, Copeland, the newest manager, was

1 doing quite well while the sector was down.
2 Year to date as a whole, small caps lag the
3 broad U.S. stock market and that's a trend
4 that was reversed by, you know, a fairly
5 large magnitude here in September.

6 The small cap stocks outperform
7 large caps by as much as 2% in the month of
8 September. So that weight's going to have
9 to benefit the plan when we see the flash in
10 ten days. International equity, down 3.3%
11 relative to the benchmark down 3.09 net of
12 fees, largely related to Acadia.

13 You can see for the month they
14 missed their benchmark, you know, by a valid
15 percent. Similarly to PineBridge, they are
16 a quantal manager. They've only been in
17 the portfolio about two months at this
18 point. So, you know, they've continued to
19 build out their positions. Within fixed
20 income for the month, you can see the top
21 there, 2.14 versus the Barklay's aggregate,
22 2.59, nearly 2.6.

23 You know, the active contribution
24 from the core and, you know, investment

1 grade credit managers was positive but not a
2 magnitude to offset the underperformance
3 caused by the intermediate managers. So
4 when I'm talking about that, I'm talking
5 about Lazard and Garcia Hamilton, you know,
6 towards the bottom there. They're
7 benchmarked to be -- Bloomberg Barklay's
8 intermediate in the intermediate group.

9 So you can see, you know, while
10 they outperform -- was already outperforming
11 as a benchmark, Garcia Hamilton was slightly
12 behind. But, you know, their benchmarks as
13 a whole underperformed the Barklay's
14 aggregate by merely a percentage point and
15 that's a trend that's persisted year to
16 date.

17 You know, from an active
18 standpoint, they've done well but it's a
19 question of, you know, do we want to
20 continue to maintain an allocation to this
21 intermediate sector of the bond market?
22 That's one that's been, you know, in place
23 quite a while here. As we move through the
24 RFPs, we've tackled a number of the themes

1 in large cap, small cap, international
2 equity.

3 You know, I think the next thing we
4 tackle is a simplification of the fixed
5 income through the issuance. It's more of
6 these consolidations and a determination of
7 do we want to, you know, retain this if we
8 hit?

9 You might recall we've made a
10 decision over the last two years to add
11 investment grade credit, to add high yield
12 which over that time has been beneficial,
13 you know, after which is the next step to
14 the fixed income portfolio.

15 I'll pass a number of -- we have --
16 updated as of September 27th, you can see
17 the market value as of this time,
18 \$550,836,605. And maintaining, you know,
19 again, if you look at the column titled The
20 Allocation Difference, it's the fourth
21 column to the right, maintaining an
22 overweight to equities, underweight to fixed
23 income.

24 Given the performance -- relative

1 performance of the asset class this year has
2 on a whole benefited the plan. You know, we
3 don't -- our views haven't changed. We
4 don't see a recession in the next six to
5 twelve months. You know, consumer spending
6 remains strong.

7 You know, I didn't really go into
8 the Rhumblin company a great deal but we
9 have accommodated a Federal Reserve policy
10 at this point and we continue to favor the
11 stock markets over the bond markets for the
12 near to intermediate term.

13 I'll open it up to questions at
14 this point for our views on the positioning
15 of the plan, no recommendations at this
16 time, we changed the asset allocation. You
17 know, we'll have a greater discussion on
18 that in a few months.

19 (No response).

20 MR. SCOTT: Do we have any
21 new business that we want to discuss at this
22 time?

23 MR. DIFUSCO: Just a couple
24 real quick announcements. And I'll be

1 cautious 'cause we have the vendors in the
2 room.

3 So I'm working through the
4 Custodial Bank RFPs. I met with one of the
5 applicants. I'll meet with another tomorrow
6 and then I'll meet with the incumbent I
7 think in about another week. My goal is to
8 have a report and a finalist or finalists to
9 present no later than the January meeting.

10 Once I'm through that report, then
11 I'll turn my attention to the RFP in the
12 process for an investment consultant. That
13 contract ends March 31st of next year so
14 I'll turn my attention to the RFP selection
15 process for that. And I'll keep the
16 commissioners certainly updated either at
17 the meetings, or depending on the
18 information, through e-mail or offline
19 communications.

20 MR. SCOTT: All right. Is
21 there a motion to adjourn?

22 MR. DUNBAR: Before we do, I
23 would like to address quickly -- to
24 congratulate my colleague, Alex, for

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1 recently getting married.

2 MR. GOLDSMITH: Thanks.

3 MS. RHYNHART:

4 Congratulations.

5 MR. GOLDSMITH: Thank you.

6 It was a very city-focused wedding, very
7 Philly. We got married over the Penn campus
8 and it was a nice party downtown. Thanks,
9 Christian.

10 MR. DUNBAR: So with that, I
11 make a move to adjourn.

12 MR. SCOTT: So moved. Thank
13 you.

14 - - -

15 (This concludes the meeting
16 at 11:10 a.m.)

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C E R T I F I C A T I O N

1
2
3 I hereby certify that the
4 proceedings and evidence noted are contained
5 fully and accurately in the stenographic
6 notes taken by me upon the foregoing matter
7 dated October 1, 2019 and that this is a
8 correct transcript of the same.
9

10
11 Amy Marzario
12 Court Reporter - Notary Public
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15 this transcript does not apply to any
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