

Sinking Fund Commission In Re: September Meeting
September 13, 2017

CITY OF PHILADELPHIA
SINKING FUND COMMISSION

In Re: September Meeting

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Wednesday, September 13, 2017

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This Meeting of the Sinking Fund Commission,
held pursuant to notice in the above mentioned
cause, before Angela M. King, RPR, Court Reporter
- Notary Public there being present, held at Two
Penn Center, 16th Floor Conference Room on the
above date, commencing at approximately 10:00
a.m., pursuant to the State of Pennsylvania
General Court Rules

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<p>1 A P P E A R A N C E S</p> <p>2</p> <p>3 COMMISSION MEMBERS:</p> <p>4 Donn Scott, Chairman</p> <p>5 Alan Butkovitz, Controller</p> <p>6 Rasheia Johnson, Treasurer</p> <p>7</p> <p>8 ALSO PRESENT:</p> <p>9 Christopher R. DiFusco, CIO, PGW</p> <p>10 Bill Rubin</p> <p>11 Alex Goldsmith, PFM Asset Management</p> <p>12 Marc Ammaturo, PFM Asset Management</p> <p>13 City Solicitor Representatives</p> <p>14 PGW Representatives</p> <p>15</p> <p>16</p> <p>17</p> <p>18</p> <p>19</p> <p>20</p> <p>21</p> <p>22</p> <p>23</p> <p>24</p>	<p>1 to -- this report covers the cash contribution</p> <p>2 requirements for the plan based on the funding</p> <p>3 policy adopted by PGW. Before we give you the</p> <p>4 report, the high level is generally speaking good</p> <p>5 news this year. On the liability side, we always</p> <p>6 look at the liabilities.</p> <p>7 We have certain assumptions of what's</p> <p>8 going to happen in the future this particular</p> <p>9 year. You know, it varies year to year. You</p> <p>10 make assumptions about how many people are going</p> <p>11 to retire, how many are going to need employment,</p> <p>12 how long people are going to live. A lot of</p> <p>13 assumptions of that nature. This particular</p> <p>14 year, the assumptions all really matched what</p> <p>15 happened in the liabilities. Variation of what</p> <p>16 we expected versus what actually happened was off</p> <p>17 by less than 1 percent. Generally speaking, we</p> <p>18 usually look for variance of 3 to 4 percent per</p> <p>19 year up and down. Because there are so many</p> <p>20 things that can happen in a year, the idea is</p> <p>21 that any one year you can be off. Generally</p> <p>22 speaking, long term you are in good shape. This</p> <p>23 particular year, we are very close to what was</p> <p>24 expected.</p>
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<p>1 - - -</p> <p>2 CHAIRMAN SCOTT: Good morning, everyone.</p> <p>3 I am delighted to call this meeting to order. I</p> <p>4 trust everyone had a great summer.</p> <p>5 First order of business is the Approval</p> <p>6 of the Transcript. Is there a motion to approve</p> <p>7 the transcript?</p> <p>8 MS. JOHNSON: So moved.</p> <p>9 MR. RUBIN: Seconded.</p> <p>10 CHAIRMAN SCOTT: Motion has been made</p> <p>11 and properly seconded. The transcript is hereby</p> <p>12 approved.</p> <p>13 The third bullet point is the actuary</p> <p>14 report and presentation. Vicente, the floor is</p> <p>15 yours.</p> <p>16 MR. VICENTE: Thank you. Do you guys</p> <p>17 have copies?</p> <p>18 (PGW Reps enter proceedings.)</p> <p>19 MS. JACKSON: Vanessa Jackson from PGW</p> <p>20 and Donna Davis.</p> <p>21 CHAIRMAN SCOTT: Good morning.</p> <p>22 MR. VICENTE: This is our annual report.</p> <p>23 The funding status of the pension plan, the PGW</p> <p>24 Pension Plan. For funding purposes, we are here</p>	<p>1 Liability side, no surprises. No</p> <p>2 problems.</p> <p>3 MR. RUBIN: Tom, what mortality table do</p> <p>4 you use?</p> <p>5 MR. VICENTE: We are using the</p> <p>6 retirement Plan 2014 Mortality Table. It's</p> <p>7 published by Society of Actuaries. That's the</p> <p>8 base table. We use a generational improvement</p> <p>9 scale called the MP 2016 Scale.</p> <p>10 MR. RUBIN: Is that age 85?</p> <p>11 MR. VICENTE: Doesn't really have a</p> <p>12 particular age. It's all statistics. If you</p> <p>13 look in expectation of life for someone age 65,</p> <p>14 it would put you in the 85, 86 range.</p> <p>15 MR. RUBIN: Okay. If you make it to 65,</p> <p>16 you make it to 85?</p> <p>17 MR. VICENTE: Good chance.</p> <p>18 (Laughter)</p> <p>19 MR. BUTKOVITZ: Feel better already.</p> <p>20 MR. VICENTE: That is the one assumption</p> <p>21 update we made this year. The base table, the</p> <p>22 2014 one we mentioned is going to be in place for</p> <p>23 several years. What they did is they update the</p> <p>24 projection scale annually in the fall, late</p>

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<p>1 October. We did update, as we did last year, 2 update the projections to keep pace with what the 3 latest findings are. That actually, it will vary 4 year to year. But this particular year, the 5 projection was such that the projection of how 6 much we are improving our longevity, so be ready 7 for it, is less than we were last year. We are 8 not projecting to do as well in the future as we 9 were projecting to do in the future a year before 10 that. 11 That actually provided gain to the plan. 12 The liability is a little bit lower because of 13 that. The expectation for improvements and 14 longevity are lower than they were a year before 15 based on the data. We are just updating that on 16 an annual basis. So, be a new one that comes out 17 late October of this year. 18 MR. BUTKOVITZ: There were people, I 19 don't know, ten years ago who were trying to sell 20 insurance product based on the old mortality 21 tables that wanted to insure all the City 22 employees. Do you have any idea whether any city 23 did that and what the results were? 24 MR. VICENTE: Not that I'm aware of. I</p>	<p>1 that through talking with PGW in asking what 2 their expectations were. And when they look at 3 their workforce and how folks are moving through 4 their careers as well as the kind of raises that 5 are being given out. 6 While the -- I think the negotiated 7 union pay scale may not be 5 percent increase. 8 When you load into that changes in rank or 9 status, you do end up with something that's close 10 to the 5 percent. We confirm that with PGW 11 before starting this year. 12 MR. RUBIN: Do you exclude the executive 13 level employees who would not increase their 14 liability to pension fund based on their salaries 15 being above the limits? 16 MR. VICENTE: Yes. Yes. So, that's not 17 a part. 18 MR. RUBIN: This is only employees that 19 would fall into the liability characterization of 20 future liabilities -- 21 MR. VICENTE: Correct. 22 MR. RUBIN: -- in the pension? 23 MR. VICENTE: Individuals who are still 24 working and earning a pension under the PGW</p>
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<p>1 don't think it was really looked at as a really 2 strong product. 3 MR. BUTKOVITZ: They made it sound like 4 we couldn't lose on it. Sounds like we would 5 have lost. 6 MR. VICENTE: Yes, they usually do. But 7 no, I'm not aware of anybody that did that. 8 There is a lot of that around retired medical 9 area where folks try to sell the bonds to insure 10 everybody's life. When people passed away, paid 11 for the post-retirement medical. I don't know 12 how many actually ever purchased that product. I 13 remember being sold or pitched, but not -- 14 MR. BUTKOVITZ: Was that ten years ago? 15 MR. VICENTE: That would have been 16 probably that time frame. 17 MR. RUBIN: Tom, what's the 5 percent 18 average pay increase based on? Is that raises 19 that are going to take effect? 20 MR. VICENTE: The increase in pay is all 21 increases. So, it's merit pay, cost of living 22 pay, promotion pay. Anything that would increase 23 pay year over year for the group, on average for 24 the group over their career. We came up with</p>	<p>1 Pension Plan. 2 MR. RUBIN: Okay. 3 MR. VICENTE: All right. If we want to 4 turn to page 1 of the report, that's the high 5 level. Page 1 we will walk through some of the 6 different numbers here. 7 So page 1 gives you some basic 8 information on the demographics. And you will 9 see there that our head count active 10 participants, those who are actively working, 11 this is a snapshot of July 1 of each year. We 12 are slightly lower active size than the year 13 before. That's to be expected given that as new 14 employees come in, they are given a choice 15 between this plan and the defined contribution 16 plan. So, there is a slip. 17 Most recently, it was about 18 three-quarters of the folks were taking this 19 plan. Previous to that, it was about half. It's 20 going to vary year to year. We are seeing some 21 different patterns there. Either way, we expect 22 if 25 percent are taking the defined contribution 23 plan, we will gradually see this group is getting 24 smaller as not every person believes is replaced</p>

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<p>1 with somebody else. Because more than half will 2 go to the plan. Eventually that will reach a 3 stability point, where the number coming in will 4 replace those going out. But we see slight 5 decreases. 6 Retirees, you will see that's down a 7 little bit. That's because there were a number 8 of individuals who passed away this past year. 9 Vested/terminated, those are folks who left 10 employment but are vested in the pension but they 11 are not yet eligible to retire for their age or 12 likely to retire as the case may be. You will 13 see there's a slight increase there. 14 In the back of the report for those who 15 are interested in that type of thing, give you 16 real turn to this. Back on page 22, there is 17 actually a reconciliation of how individuals went 18 from one point to the other. So, that gives you 19 an idea of about what the ins and outs were so to 20 speak for the categories. 21 You see payroll there up about 22 4 percent. Average pay about 5 percent. Again 23 this particular year, it matched pretty well what 24 our assumption was. In other years, you will see</p>	<p>1 down by years of service on a graphing basis. 2 Even though the average is 15 years of service, 3 you will see that we have more people in the 5 to 4 10 years of service group than any other group. 5 Which you would expect with turnover, generally 6 that type of thing. You will generally see more 7 of the service agents that spread out farther to 8 the right. A little bit of a dip there between 9 15 and 25 years of service. You will see that 10 change over time. 11 That gives you an idea how to come up 12 with the 15. That's how it's distributed. The 13 average can be a little bit misleading as most 14 people are either well below or well above that, 15 but they average that 15 years. 16 MR. RUBIN: Distribution of inactive 17 participants. So that's -- 18 MR. VICENTE: On page 19? 19 MR. RUBIN: Yeah. What's the inactive? 20 That's somebody who is -- 21 MR. VICENTE: What we have here are the 22 top table of those receiving benefits. Those are 23 who are either retirees themselves or 24 beneficiaries of retirees.</p>
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<p>1 it be higher or lower. Average age stayed pretty 2 steady as did average past service. Both good. 3 And part of the reason why, we kept actuarially 4 pretty sound or pretty level everything. Nothing 5 changed that much. That's the demographics. 6 MR. RUBIN: The average past service, 7 that means that most people are serving 15 years 8 and retiring? 9 MR. VICENTE: That's just the average 10 service of the group that's in place right now. 11 That was 1,243 individuals who were working there 12 today. That's their average service. 13 MR. RUBIN: So, there could be a longer 14 service which would be higher liability? 15 MR. VICENTE: Exactly. 16 MR. RUBIN: Okay. 17 MR. VICENTE: If you turn back to page 18 19 of the report, you can see -- actually, it's 19 page 20 really. Is the -- a big chart on page 20 20 that shows you how much -- what people fall for 21 in terms of on the vertical axis. It's their 22 ages. In the horizontal axis is their years of 23 service. Graphically, if you turn to the next 24 page, page 21, you can see how the group breaks</p>	<p>1 MR. RUBIN: Okay. 2 MR. VICENTE: That gives the idea of how 3 long they have been in pay status based on age. 4 You will see some very young people that would be 5 beneficiary clearly of somebody or perhaps sort 6 of disability. And the bottom table, the vested 7 terminated, those are those folks who have left 8 the Authority or the Gas Works but have not yet 9 started their pensions and how old they are. 10 There are a few. There are five over 11 age 65. So from an administrative standpoint, 12 the idea we get them in pay status as soon as 13 possible since they are at their full retirement 14 ages. Chances are if there are only five of 15 them, they are probably who we have trouble 16 locating and that is why they haven't started 17 yet. What happens, people leave and 20 years 18 later you are trying to find them to get their 19 pension started. They may have left the country 20 for all we know. 21 MR. RUBIN: On 20, when you have the 22 number and -- is that dollar amounts underneath 23 that? 24 MR. VICENTE: The number is the head</p>

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<p>1 count. On the first cell on the 20, the top 2 left, you will see 16. There are 16 individuals 3 there. And the average pay of those 16 4 individuals is the \$38,240. 5 MR. RUBIN: Average pay? 6 MR. VICENTE: Right. 7 MR. RUBIN: Not pension? 8 MR. VICENTE: Correct. Average pay. 9 MR. RUBIN: Thank you. 10 MR. VICENTE: That's a lot of the 11 demographic information. If we turn to page 2 of 12 the report, you see some of the financial metrics 13 for funding purposes. 14 The first item is what is called the 15 Normal Cost. That's the cost allocated as a 16 group for those individuals who are actively 17 working. How much does it cost to pay for the 18 benefit they earn from working a year? In this 19 case, \$7.7 million, which is roughly 9 percent of 20 payroll. 21 So if you think about the cost of this 22 plan on a long term basis, if you are a hundred 23 percent funded, the plan would have a cost above 24 9 percent pay. You are paying just the normal</p>	<p>1 expectation? 2 MR. RUBIN: -- if they live longer? 3 MR. VICENTE: Because we expect the 4 change in the projection scale reduced the level 5 of improvement in longevity. We actually are 6 assuming now people are going to live a little 7 less long than they did last year. That factor, 8 that improvement scales updated every year. We 9 will have a tweak upwards or downwards every 10 year. Should be relatively small overall. 11 That's the main outcome there. When you 12 turn to the next page, you will see some of the 13 liability figures at the top. The unfunded 14 liabilities is about \$217 million. And that's on 15 a cumulated liabilities for about just under 16 \$700 million. We are about 70 percent funded 17 overall on the plan. 18 If we turn to the next page, page 4, we 19 show the asset values. We have two values there 20 on page 4: The market value and the actuarial 21 value. 22 The market value is just what you would 23 expect. We take -- look at the actual investment 24 statements and pulled a number off there. This</p>
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<p>1 cost, the cost that is being earned in a 2 particular year. Below that you will see the 3 contributions schedules. The policy adopted by 4 PGW is to use the larger of what's called the 20 5 Year Contribution or the 30 Year Contribution. 6 In this case, it's the 20 Year Contribution. 7 About \$28 million this year, which equates to 8 just under 30 percent of payroll. 9 We expect the 20 Year Contribution to be 10 the dominant contribution method for the next 10, 11 15 years. And then gradually the 30 Year 12 Contribution method will overtake it because of 13 the mechanisms involved there. That is policy 14 that was adopted, I think, two or three years ago 15 by the Board as a way to determine the 16 contribution. 17 About a 3 percent decrease from the 18 prior year. That goes to the fact that the 19 investments did relatively well. The change in 20 the mortality expectation helped to bring that 21 down, as well. 22 MR. RUBIN: How does that help to bring 23 it down if the -- 24 MR. VICENTE: The change in mortality</p>	<p>1 is a preliminary market value. So, we get the 2 value from a flash report from the Sinking Fund 3 and working with PFM. However, when the auditor 4 goes through and completes the audit or 5 financials for the plan, there could be a small 6 upward or downward change in that. That is still 7 in the case, we have seen some preliminary audit 8 financials just this last week. They are a 9 little bit different. About less than 1 percent 10 different. So, we will refine this report once 11 we get the final audited financials. Basically, 12 the difference right now, we don't expect there 13 to be anything material in terms of a change of 14 the outcomes. 15 The actuarial values, again methodology 16 adopted a couple of years ago. And what that 17 does is essentially averages in investment 18 returns that are above or below the 7.3 percent 19 assumed return. So, we have a higher return than 20 assumed, than we don't actually recognize all of 21 that in the first year. We phase it into the 22 asset value over a couple of years. On the same 23 token, if we return less than 7.3 percent in the 24 year, we phase that loss in.</p>

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<p style="text-align: right;">Page 18</p> <p>1 The idea is that over a three or four 2 year period, the period will exceed and miss will 3 average out and keep the asset value a little 4 smoother, which will keep the contributions level 5 a little smoother. At the same time, not letting 6 us deviate too much from where we really sit. 7 That is a method we adopted several years ago. 8 You see this particular year, they are 9 very close together, closer than they were last 10 year. This year we returned, I want to say, 11 about a 12 percent return which is much higher 12 than the 7.3 a year before that. We had almost a 13 0 percent return or so. Those two are more or 14 less offsetting when you look at this particular 15 year, which is why the two numbers are so close 16 together. 17 CHAIRMAN SCOTT: Would you expect it to 18 be -- is it better when it is closer together or 19 versus a negative variance? 20 MR. VICENTE: I mean, yes. If they stay 21 relatively close together, that means our 22 assumption is pretty good as far as modeling what 23 the returns have been in the past, which gives us 24 a good outlook for the future. If they are</p>	<p style="text-align: right;">Page 20</p> <p>1 probably the next page to look at is just on page 2 10 of the report. Just have graphically shown 3 the two contribution levels. I can go through 4 every page of the report, but a lot of it is 5 actuarial mathematics. I'm not sure if everybody 6 wants to do that. I enjoy doing it, but not 7 everyone wants to hear it. 8 Page 7 gives you graphically how the 9 contributions are made up. We mentioned that 10 normal cost figure, which is 9 percent pay. 11 That's the orange or red there. The blue bottom 12 is the amortization. We are paying off that 13 \$200 million unfunded liability. That's how 14 much -- you can see a large portion of annual 15 contributions is paying down what's unfunded due 16 to past service. 17 And a lot of the unfunded that we have 18 right now came about from a number of sources. 19 So certainly if you go back far enough, you'll 20 find this plan had been a hundred percent funded. 21 But some of the investment ups and downs 22 beginning in 2008 affected the plan as it did 23 most pension programs. And on top of that for 24 this plan, as you recall, we actually reduced the</p>
<p style="text-align: right;">Page 19</p> <p>1 persistently higher or persistently lower, it 2 means we are either being too aggressive or too 3 conservative in our assumption. Either way, with 4 a plan like this, there is no getting away from 5 the actual cost of the plan. 6 So you know, if we are being too 7 aggressive with our assumption, for example, and 8 assuming 7.3 when really we should be thinking 9 something lower than that, it will come back. It 10 will just be a timing issue that we will have 11 lower contributions initially. But as the 12 effective lower returns makes itself felt, we 13 will catch up. And vice versa. 14 If we are too conservative, we will have 15 higher contributions initially. But then as the 16 higher returns make themselves evident, we will 17 see our contributions come down. So it's more 18 about backloading and front loading. Ideally, we 19 are not doing either, and that's a good sign that 20 we are relatively close. But we will likely see 21 it fluctuate up and down every year. That is 22 what you expect in the investment makeup, which 23 includes some fairly volatile type of return. 24 Flipping forward a couple of pages,</p>	<p style="text-align: right;">Page 21</p> <p>1 expected long term rate of return several times 2 over the last four or five years. 3 And that's -- when you look at this, we 4 changed the liability based on the expectation 5 for how, what kind of return rate we are going to 6 get on that. When you make that change, that 7 creates a liability you haven't funded for. You 8 thought of previously with the higher rate, you 9 are essentially implying that investment returns 10 will pay that off. Once you lower the investment 11 return assumption, you are saying the investment 12 won't pay that off. Instead contributions will 13 pay that off. 14 MR. DIFUSCO: Tom, I think you mentioned 15 this last year when you were here. We also had 16 that one year or two-year spike in retirements 17 which I think also added a couple percentage 18 points to the unfunded, as well. 19 MR. VICENTE: That is true. Experience 20 deviating from what we expect. 21 As we go forward to page 12, page 12 22 shows the cash payouts of the plan. Our 23 expectation based on our assumption about 24 retirements and new hires and pay increases and</p>

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1 so forth translates to a certain pay amount being
2 paid out of the plan to cover participants
3 benefits as they retire. You will see there, we
4 are expecting about \$53 million for the year that
5 just began this past July. Increasing gradually
6 to about an extra \$10 million per year about ten
7 years from now. That's based on the age of the
8 group and the size of their salary and service
9 and what kind of pension we expect to get. That
10 gives you an idea what the outflows would be for
11 the plan.
12 MR. BUTKOVITZ: So, that's assuming that
13 the payments would go to their spouses?
14 MR. VICENTE: Correct. We have an
15 assumption about how many people will -- what
16 kind of benefit option folks will take.
17 MR. BUTKOVITZ: What's the assumption?
18 MR. VICENTE: I don't -- I have to look
19 it up for you. We have an assumption based on
20 what the pattern has been in the past. It's
21 usually -- with this group, I imagine it's
22 relatively high percentage assumed to take the
23 survivor benefit. This is a male dominated
24 workforce. And men generally tend to take

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1 benefits that cover their spouses. Historically,
2 that's because their spouses generally didn't
3 have a job or were more at home. They didn't
4 have another source of income versus when you
5 have female dominated workforces, the husband
6 generally has a job. It's less trend to take
7 that. Not universal, but that's the trend.
8 If we turn to page 13, you have a
9 historical review of the funded progress of the
10 plan. So, the bars represent the liability.
11 That's our projection of the current liability of
12 the group. You see that historically from 2009
13 to 2017. And you will see some places where
14 there are jumps. And those jumps do correspond
15 to where the assumed rate of return was changed.
16 And then the blue line is the market value plan
17 assets as compared. You see that goes through.
18 In black, we have the percentage funded. You are
19 seeing 70.6 percent funded currently, which is
20 improvement by about 5 percent over where it was
21 in 2016.
22 Nice little pick up there making up most
23 of what we gave away last year when we changed
24 the assumed rate of return from 7.65 down to 7.3.

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1 You will see that's a increase in 2016 as we made
2 that change. The investment returns this year
3 were, again, close to a 13 percent return. You
4 can see how that's trended over the last decade
5 or so.
6 CHAIRMAN SCOTT: So, what happened in
7 '14 and '15? What's responsible for -- it was 80
8 percent funded in '14?
9 MR. VICENTE: Right. The big -- one big
10 thing there was went from a 7.95 percent assumed
11 rate of return down to a 7.65 percent return. 30
12 basis points decrease in our assumed rate of
13 return. That boosts the liability up. We also
14 had at that point in time, that was right around
15 the time I think a lot of the sale discussions
16 were going on. And that's when we did have a lot
17 of individuals sort of rush to the door a little
18 bit earlier than otherwise projected. So, that
19 increased the liability as well.
20 MR. DIFUSCO: Tom, when you list the
21 funded ratios for the past years, have they been
22 adjusted in the sense that, you know, we had --
23 we weren't using smoothing then and we were doing
24 other things. Or you just using the returns that

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1 are in the older reports with the then, like, all
2 the same assumptions?
3 MR. VICENTE: It was the assumption that
4 were in place at that time.
5 MR. DIFUSCO: Okay. That would affect,
6 I mean, the numbers and how the gap looks as well
7 because there's not a smoothing affect. There's
8 not --
9 MR. VICENTE: Right.
10 MR. DIFUSCO: That's what I thought, but
11 I just wanted you to confirm.
12 MR. VICENTE: That's what we have there.
13 If we flip forward a couple of other pages to
14 page 16, page 16 is this. If I was looking back,
15 page 16 is looking forward.
16 Page 16 is our projection of cash
17 contribution and how the fund levels is going to
18 progress in the future. So, the table at the top
19 and then the bottom we have a chart showing the
20 same information. And because this is a
21 projection assuming that all our assumptions are
22 going to come true absolutely every single year,
23 it shows this very nice pretty picture with a
24 very straight line of the investment with the

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<p>1 funded ratio improving every year very gradually. 2 In real life, we will see ups and downs. Real 3 life won't show this way. We will have years 4 like this year, 13 percent return. We will have 5 years like two years ago where we have 0 percent 6 investment return. Years where the pay increases 7 are flatter and years where the pay increases are 8 more. So, we will see ups and downs there. 9 But assuming everything goes along, our 10 plan and this verifies our funding policy, is to 11 fund the plan over 20 to 30-year period. And 12 that is why you see this gradual increase in the 13 funded ratio. Seems like it's taking forever to 14 go from 70 percent to 78 percent. But that is 15 the nature of funding this on a long term basis. 16 In the middle of the table at the top, 17 you will see a column, Type of Actual Mid Year 18 Contribution. So, that's telling you what the 19 cash contributions are expected to be. Again, 20 making certain assumptions about the workforce. 21 So here, we are assuming that -- I believe we are 22 assuming that three out of every four new hire 23 comes into this plan versus going to the Defined 24 Contribution Plan. So, that's driving the</p>	<p>1 the other assumptions stay the same, which are 2 the -- our assumptions about when people retire 3 as far as age and length of service, when they 4 will leave voluntarily is based on PGW's actual 5 experience. 6 We update that experience and study 7 every three to five years. I think it's been 8 three years since we did it. Probably next year 9 we will talk to PGW about whether we should 10 update that study, see if we validate whether the 11 assumptions are still working as expected. If 12 there are any trends emerging and update it from 13 that point of view. But for right now, we are 14 using that same assumption because we haven't 15 come to the point. 16 As you saw when I mentioned, the 17 liabilities turned out to be pretty close to what 18 we expected. We are not seeing any indication 19 that we are having a real deviation right now. 20 Again, it's good practice. Next year we will 21 start talking about do we need to do a new study 22 or review those assumptions. 23 No changes in Plan Provisions from last 24 year. Everything stayed the same there in terms</p>
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<p>1 contribution to some extent. 2 This is our projection. You do see the 3 contribution level rate amount does go down year 4 to year. That's partially as a consequence, even 5 if you are replacing three out of four, there is 6 one person you're not replacing as they go into 7 the other plan. And that is where that cost 8 shows up, in the other plan, not this plan. 9 The next two pages we don't go into 10 detail. But they show the two different 11 methodologies, the 20 Year Method and the 30 Year 12 Method. You can see how they vary one versus the 13 other. If you held them side by side, the 20 14 years is the dominant method for most of the 15 period. But as you get into 2024 and 2025, the 16 30 Year Method starts to take over just by the 17 nature of the mechanics. Two different methods. 18 Then we already talked about the 19 information on pages 19 through 22, our 20 demographic information. So we don't have to do 21 that again. The next section starting on page 23 22 is all our methods an assumptions as we 23 mentioned. The only assumptions we change this 24 year was the mortality improvement scale. All</p>	<p>1 of cost. 2 So, that's the report. I don't know if 3 there are any other questions you want to ask. 4 Nothing? Thank you. 5 MR. RUBIN: Thank you. 6 MS. JOHNSON: Thank you. 7 CHAIRMAN SCOTT: Thank you very much. 8 MR. DIFUSCO: Thanks, Tom. 9 CHAIRMAN SCOTT: Next item on the Agenda 10 is the PGW Pension Plan Investment Consultants. 11 MR. GOLDSMITH: Thank you. 12 I will make some brief comments on the 13 markets and economy. And in your binder, you 14 have the flash performance as of July 31. The 15 August performance is ready typically about ten 16 business days after the quarter end because of 17 the start timing of September with Labor Day. We 18 are at eight business days today. By Friday 19 afternoon, we will have that distributed to you, 20 all the August flash performance. 21 But just briefly speaking to markets and 22 economy, I think if you followed markets this 23 year, the story continues that it's been a good 24 period for equities. Domestic equities are up,</p>

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<p>1 you know, year-to-date as of yesterday about 2 12 percent. International equities leading about 3 20 percent year-to-date. And large cap stocks 4 outperforming small caps. Another brief trend I 5 will note, growth stocks and sectors, healthcare, 6 information technology outperforming value stocks 7 and sectors.</p> <p>8 With the performance of the markets 9 here, I get questions about overvaluation and do 10 we think markets are overvalued? You know, 11 certainly looking at the data, price-to-earnings 12 being a major metric of valuation, U.S. stocks 13 are higher than their long term valuation rates. 14 S&P 500, 18 times; price-to-earnings times 16. 15 That ratio has been relatively consistent 16 year-to-date.</p> <p>17 Earnings growth, earnings per share 18 growth in the second quarter was 16 percent. So, 19 prices are certainly up with going back to the 20 the election of Donald Trump last year and 21 really, you know, seven years ago to the recovery 22 from the financial crisis. But as long as, you 23 know, corporations here in the U.S. have 24 delivered positive results, positive earnings,</p>	<p>1 started the year undervalued relative to U.S. 2 stocks and performed well as a result.</p> <p>3 I'll briefly speak to the fixed income 4 market because of additional challenges, you 5 know, lie ahead there. Rates certainly shot up 6 following the election. We have very weak fourth 7 quarter last year for fixed income returns. On 8 the margins this year, long term rates have 9 fallen slightly while short term rates have 10 increased. Bit of a flattening in the yield 11 curve, which in turn has supported equities. The 12 Fed still indicates that they intend to act at 13 least one more time to raise rates this year with 14 the economy doing better. It's looking like that 15 will take place.</p> <p>16 Again as interest rates rise, the impact 17 on existing bond prices is such that it forces 18 those down. So certainly, challenges they had, I 19 think, for fixed income.</p> <p>20 Focusing on the report here very 21 briefly, page 1, you can see the market value as 22 of 7/31, 522 million, so up slightly from the 7.1 23 figure that Tom presented. The one month return 24 was right on top of the benchmark slightly above</p>
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<p>1 that, you know, the overvaluation that we have 2 seen has remained in check.</p> <p>3 I think what's interesting to note 4 that's emerged over the last month or two that 5 has injected some volatility in the market has 6 been geo political concerns, mostly related to 7 North Korea. Certainly, there was an episode in 8 early August and then about a week ago with the 9 test of the hydrogen bomb. You know, again, 10 volatility which had been near record lows for 11 most of 2017 went up 12 percent but still remains 12 fairly low. And you know, I think despite, 13 again, a bit of negative return in some sectors 14 in August, U.S. markets hit record highs 15 yesterday with both the Dow and the S&P 500 16 simultaneously hitting record highs. Now, they 17 are off again slightly today.</p> <p>18 But with consumer confidence up, 19 strength in the housing market, strength in U.S. 20 corporations, certainly unemployment has fallen 21 now 4.4 percent. Our view for the intermediate 22 term here in the U.S. is positive. Certainly, 23 international markets have done a little bit 24 better. Get primarily based on valuation. They</p>	<p>1 after investment management fees. Year to date, 2 it's nice to see moving over several columns 3 about 60 basis points of outperformance 4 year-to-date. And 25 basis points or so the one 5 year number. The single greatest contributor to 6 that outperformance for year-to-date numbers been 7 in the one year has been overweight to equities. 8 Certainly with fixed income returns, delivering 9 very, very low absolute numbers, you know, the 12 10 to 15 percent depending on domestic international 11 is certainly outweighing at that. The overweight 12 is delivering the greatest amount of 13 outperformance.</p> <p>14 That being said, again, some active 15 manager, at least on the year-to-date, you know, 16 basis active management has outperformed.</p> <p>17 MR. AMMATURO: Just to interject there 18 on the application just to amplify that, numbers 19 behind what Alex just said. If you look at large 20 cap and small cap and the percent column, you add 21 those two numbers up, that's 47 percent; 22 39 percent large cap, 8 percent small cap. That 23 is 47 percent. Your target is 45. So, just to 24 put numbers behind what Alex is saying, that</p>

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<p>1 2 percent overweight to domestic equity has 2 helped. If you look down to international 3 equity, you have 21 percent international equity. 4 Your target is 20. That's 3 percent overweight 5 to equity markets. It's 2 percent domestically, 6 1 percent internationally which I would say has 7 been beneficial and tailwind to your portfolio. 8 We don't recommend rebalancing back to target at 9 this time. 10 MR. GOLDSMITH: Some of the highlights 11 within the active managers. Certainly, 12 O'Shaughnessy for the quarter as well as year to 13 date. They have benefitted from that flattening 14 of the yield curve with long term yields for 15 bonds falling. They, basically, look at one 16 metric in building their portfolio. That is 17 total shareholder yield, stock buy backs and 18 dividend payments. And those high dividend 19 stocks have really benefitted year-to-date. 20 It's not necessarily quality buys, but 21 looking for high yielding stocks. And so despite 22 challenges to the value market, O'Shaughnessy 23 delivered there. 24 I want to touch on some negative</p>	<p>1 international. The one exception is fixed 2 income. And I think that again owes to some 3 challenges presented thus far in 2017 following, 4 you know -- following a sharp rise in the rates 5 to end the year. Interest rates ameliorated 6 slightly before, again, this recent flattening of 7 the yield curve. And I think that has thrown, 8 you know, a challenge to a number of the active 9 fixed income managers. 10 That being said, over the one-year 11 number, you know, more characteristic 12 outperformance of fixed income. A steady, you 13 know, call it 1 percent or so of outperformance. 14 That is the steady months and quarters of 15 outperformance. 16 So you know, again, we are not 17 recommending any change to the positioning. I 18 believe we passed around a rebalancing page as of 19 yesterday, excuse me, as of Monday evening. The 20 plan market value is up to 529 million. Again, a 21 2.79, 2.8 overweight to equities, 1.8 percent 22 underweight to fixed income and a percent 23 underweight to cash. Again, underweight those 24 cash and fixed income sectors, overweight</p>
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<p>1 performers. I think the most important being 2 Vaughan Nelson again. Year-to-date they have 3 lagged a little bit certainly over the one year 4 number. The fact they have struggled to their 5 value positioning, but also even in addition to 6 that and underweight or, excuse me, selection 7 with industrials overweight to industrials, you 8 know, so they are really -- they are squarely in 9 their style buckets, but it's been one that's 10 underperformed. It's been offset somewhat by an 11 overweight in healthcare I talked about how 12 healthcare tax sectors have done well. But it's 13 very slight overweight. 14 One exception that I think I would say, 15 you know, as a whole I talk about -- if you look 16 at the black lines on this report, you go out to 17 the year-to-date column, you know, the combined 18 large cap figure 12.84 versus 11.44. That is why 19 I am saying that active management has 20 outperformed in that sector. That doesn't take 21 into account overweights or underweights. That 22 is just purely roll up of the manager. 23 Year-to-date outperformance in large 24 cap, outperformance in small cap, outperformance</p>	<p>1 equities. We continue to as, you know, we view 2 rises in markets -- in the markets continuing, we 3 continue to source benefit payments from 4 equities. We are not continuing to go 5 underweight to fixed income again. Evaluations 6 are high. There are some geopolitical risks 7 certainly out there. So, we are not advocating 8 going any higher but looking to take profits as 9 needed, you know, from where a performance has 10 been good year-to-date. 11 MS. JOHNSON: I have a question. We've 12 been going back to Vaughan Nelson. I mean, you 13 look at their five-year numbers and they are 14 probably where they should be. But look at three 15 year, one year, there is a trend. 16 Is there a recommendation, or should we 17 just kind of be looking to see, you know? 18 MR. GOLDSMITH: Vaughan Nelson has not 19 been placed on Watch List. It's really recent 20 underperformance has caused a lot of those 21 trailing numbers to look, you know, bad. It's a 22 slight miss over the three years. 23 MS. JOHNSON: Right. I will say, it's 24 not significant.</p>

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<p style="text-align: right;">Page 38</p> <p>1 MR. GOLDSMITH: But we like to see 2 outperformance over three. Certainly, over the 3 five years a full market cycle, that is what we 4 like to evaluate. So far, there has been no 5 change to the investment team or their process. 6 Certainly, in what's been a struggling climate 7 for value investors, we would like to see maybe 8 some of their -- given some to like let 9 investment theses play out, particularly again 10 overweights in selection within industrials where 11 they have historically exhibited good selection 12 ability. 13 So, they are not on a watch list at this 14 time. Again, I think we are not -- we don't want 15 to churn some managers when there is, you know, 16 just a certain brief periods of underperformance 17 more recently. 18 That concludes statements on this 19 report. I passed out the rebalance sheet. No 20 recommended changes to this allocation at the 21 time -- at this time. You know, I recall, I 22 think two meetings ago we approved an allocation 23 to Pinebridge on the domestic equities side to 24 replace Fred Alger and O'Shaughnessy with a less</p>	<p style="text-align: right;">Page 40</p> <p>1 know -- I note this morning I took a look at the 2 total fund AUM. It's about 530.6 as of this 3 morning September 13. And we have about 4 7.6 million in cash because we moved the money 5 following the benefit payments. These numbers 6 Alex provided are post September benefit 7 payments. We have already made that payment for 8 the month and are still around 530, 530 and a 9 half. 10 MR. RUBIN: Alex, do you have any idea 11 what the Fed is going to do? 12 MR. GOLDSMITH: Statement indicates one 13 rate hike likely in 2017. You know, I think -- 14 you know, originally if you had asked me at the 15 beginning of summer, I would have probably said 16 indications at least one. Maybe in September, 17 definitely by December. 18 I think the -- September is looking 19 slightly less likely than it did, you know, a few 20 months ago. Inflation expectations have come 21 down again slightly, long term rates have come 22 down. So that being said, I mean, the economy is 23 doing very well. The Fed looks at the health of 24 the economy outlook for inflation and then</p>
<p style="text-align: right;">Page 39</p> <p>1 volatile core active approach, and then some of 2 those assets would go into domestic equity. I 3 believe we are still waiting on contract. 4 MR. DIFUSCO: Yeah. Contract, actually, 5 I think -- we talked yesterday. Went out for 6 signatures this week. I anticipate that change 7 being made relatively soon. 8 MR. GOLDSMITH: And you know, again, 9 without any indication of August performance with 10 the active manager, I do have the benchmark 11 performance for the month of August. The 12 benchmark was up 0.51 percent. Half a percent. 13 It's reasonable to expect that, again, the fund 14 was generally close to that. You know, I 15 received some early discussions with active 16 managers. Nothing official. Nothing I can hand 17 out. It was about a mixed bag with half the 18 managers underperforming by slight amounts, some 19 good active outperformance from the equity side 20 and a lot of the fixed income managers were right 21 on top of the benchmark, net of fees. 22 We will see again on Friday. You will 23 receive an updated report. 24 MR. DIFUSCO: The only slight, you</p>	<p style="text-align: right;">Page 41</p> <p>1 unemployment. Unemployment is ten year low at 2 4.4 percent. GDP growth was 3 percent in the 3 third quarter. Pretty significant compared to 4 recent numbers. 5 So I would -- if not September, most 6 certainly but very likely that December. And I 7 think it's one more rate hike of 25 basis points. 8 It's a slow and steady climb for interest rates 9 ahead. They are not going to shoot up to 10 5 percent overnight. You know, if U.S. remains 11 really at the peak globally for interest rates, 12 Australia has been the only country with higher 13 relative rates than we do. 14 MR. RUBIN: Do we have any impact in our 15 portfolio with the devastation and the terrible 16 storms that have hit two parts of the country? 17 MR. GOLDSMITH: You do have some 18 exposure to U.S. rates through the index funds in 19 the portfolio. You know, broadly -- you know, I 20 am involved in the real estate market as well for 21 other coverage of other funds. You don't have 22 any dedicated real estate funds. Indication in 23 Houston was, I think, you know, generally 24 positive for the core properties that these own.</p>

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<p>1 Actually, I think a lot of what happened this</p> <p>2 past week in the U.S. markets, the second</p> <p>3 Hurricane Irma missing Miami where a lot of U.S.</p> <p>4 do have some investments mostly in apartments and</p> <p>5 multifamily units. I think, frankly, the</p> <p>6 hurricane shifting westward slightly is why we</p> <p>7 hit record highs a little bit yesterday to some</p> <p>8 extent.</p> <p>9 MR. AMMATURO: What percent of the index</p> <p>10 reaches a small component of the index?</p> <p>11 MR. GOLDSMITH: It's 4 percent maybe or</p> <p>12 less, 3.6 percent.</p> <p>13 MR. AMMATURO: His comments pertain to</p> <p>14 your exposure to RhumbLine and your exposure to</p> <p>15 Northern Trust. Again, we are talking about 3 to</p> <p>16 4 percent of index fund is in publicly traded</p> <p>17 real estate.</p> <p>18 MR. GOLDSMITH: Again, more broadly, I</p> <p>19 think the people had increased expectation for</p> <p>20 devastation in South Florida. And that not</p> <p>21 happening is, it's odd to say, it's almost like</p> <p>22 an upside, an unexpected upside.</p> <p>23 MR. RUBIN: If there can be any.</p> <p>24 CHAIRMAN SCOTT: We don't have exposure</p>	<p>1 that pay dividends. They are viewed as value</p> <p>2 stocks within financial component. You have a</p> <p>3 subsector that is insurance company. You do.</p> <p>4 Too early to tell what the ramifications</p> <p>5 are in terms of economic impact of those</p> <p>6 companies, but definitely have exposure. It's a</p> <p>7 small exposure.</p> <p>8 MR. RUBIN: On the other side, if there</p> <p>9 are going to be any good things that are coming</p> <p>10 out, the employment rates will probably drive up.</p> <p>11 People hired to go down there and work. And they</p> <p>12 are going to need supplies and things to rebuild.</p> <p>13 So, are we invested in companies and firms that</p> <p>14 are going to be a part of the timber or any of</p> <p>15 the other things that are going to generate</p> <p>16 there?</p> <p>17 MR. GOLDSMITH: Again, similarly, I was</p> <p>18 the broad index exposure. Also, I mentioned</p> <p>19 industrial overweights and selection. I think</p> <p>20 Vaughan Nelson being major. That's a small cap</p> <p>21 value manager. And so, a lot of the -- to the</p> <p>22 extent that there are smaller public companies</p> <p>23 that are engaged in reclamation, certainly</p> <p>24 building products, materials, there are a lot of</p>
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<p>1 to short side?</p> <p>2 MR. GOLDSMITH: Sorry?</p> <p>3 CHAIRMAN SCOTT: Do we have any exposure</p> <p>4 on the insurance side firms that provide</p> <p>5 insurance coverage for these homes?</p> <p>6 MR. GOLDSMITH: Again, certainly, I</p> <p>7 think through the index funds, you would have</p> <p>8 exposure to major U.S. insurers. And most</p> <p>9 likely, I think, O'Shaughnessy obviously being a</p> <p>10 valued investor would have allocation to</p> <p>11 financial stocks and sectors. So it's most --</p> <p>12 market weight exposure there in those sectors.</p> <p>13 You know, I think frankly it's a little</p> <p>14 early. I know that there is big port -- we were</p> <p>15 talking before the meeting, a big portion of</p> <p>16 uninsured people down in Texas. Everything that</p> <p>17 I read, it said will take a while for the full</p> <p>18 impact of that. And I guess the mechanics of how</p> <p>19 that debt gets unwound will come out.</p> <p>20 MR. AMMATURO: You undoubtedly do have</p> <p>21 exposure to your index funds to insurance</p> <p>22 companies. Then again, to support what Alex</p> <p>23 said, O'Shaughnessy tends to buy value stocks.</p> <p>24 And a lot of financial services are value stocks</p>	<p>1 innovation happening here in the U.S in</p> <p>2 interesting developments and materials. There</p> <p>3 are a lot of smaller companies.</p> <p>4 To the extent that, again, they have an</p> <p>5 overweight and they've typically over long</p> <p>6 periods exhibited good selection in those</p> <p>7 sectors, I would expect there is some allocation</p> <p>8 again to those types of companies, certainly</p> <p>9 Caterpillar. To the extent that this moves the</p> <p>10 needle for the global giant there, there is also</p> <p>11 exposure on the large cap side. Similar</p> <p>12 companies like Home Depot -- Home Depot has</p> <p>13 struggled this summer. Home Depot struggled</p> <p>14 year-to-date. Just they have caught -- retail</p> <p>15 companies as a whole have struggled. You</p> <p>16 certainly wouldn't expect a building product</p> <p>17 supplier like Home Depot. You can't really get</p> <p>18 that from Amazon. They struggled as well by</p> <p>19 virtue of being in the retail sector. This may</p> <p>20 be a catalyst for some improvement for them.</p> <p>21 Again, it's just one area or one</p> <p>22 somewhat broad region of the country. There is</p> <p>23 still, you know, large swath of people that</p> <p>24 aren't impacted by hurricanes. We have seen</p>

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1 earthquakes in the last two weeks. We have seen
2 forest fires. Again, fortunately nothing that
3 has injected too much fear into the markets.
4 Again, we didn't hit record highs yesterday. So,
5 it's pretty early. But I think over the long
6 term neutral to positive outlooks based on those
7 storms despite, obviously, the destruction and
8 loss of life.

9 CHAIRMAN SCOTT: Any other questions?

10 Any new business for us to discuss this
11 morning.

12 MR. RUBIN: Motion to adjourn.

13 MS. JOHNSON: I second.

14 CHAIRMAN SCOTT: Done. This meeting is
15 hereby adjourned.
16 (Sinking Fund Meeting adjourned at 10:49 a.m.)
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C E R T I F I C A T I O N

I, hereby certify that the
proceedings and evidence noted are
contained fully and accurately in the
stenographic notes taken by me in the
foregoing matter, and that this is a
correct transcript of the same.

ANGELA M. KING, RPR
Court Reporter - Notary Public

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