CITY OF PHILADELPHIA
BOARD OF PENSIONS AND RETIREMENT
Meeting of February 23, 2012

MINUTES

On February 23, 2012, Paula Weiss called the Regular Meeting of the Board of Pensions and Retirement to order at 9:13 a.m. in the Board's Conference Room.

Present:	Rob Dubow Paula Weiss Alan Butkovitz Brian Albert Celia O'Leary Carol Stukes Ronald Stagliano John Reilly Veronica Pankey Hilary Cornell James Leonard Anne Kelly King
Also Attending:	Francis Bielli, Mark Murphy, Shamika Taliaferro – Board of Pensions Christopher DiFusco, Benjamin Hinerfeld – Law Department Sumit Handa, Brad Woolworth – Board of Pensions, Investment Unit Andrew Thomas – Fire Department Kevin P. Norton – BNY Mellon Warren West – Greentree Tina Williams – FIS Group Bill Rubin – Citizen Wayne Pollack - Citizen Ken Kent, Karen Zangara, Anu Patel – Cheiron

Paula Weiss stated that the first order of business was the consideration of the Minutes of January 26, 2012.

John Reilly made a motion to approve the Minutes of January 26, 2012. Brian Albert seconded the motion.

The motion to approve the Minutes of January 26, 2012 carried unanimously 7-0.

CONSIDERATION OF (92) PENSION APPLICATIONS AND (56) WITHDRAWAL APPLICATIONS

Brian Albert made a motion to approve. Ronald Stagliano seconded the motion.

The motion to approve carried unanimously 7-0.

APPLICATIONS FOR SERVICE-CONNECTED DISABILITY BENEFITS

Case of Richard DeCoatsworth, Application for Service-Connected Disability Benefits - Plan "B".

This is an application by Richard DeCoatsworth, former Police Officer, for Service-Connected Disability Benefits in Plan "B".

Mr. DeCoatsworth sustained gunshot injuries while working when he was shot in the face while apprehending a suspect. His date of injury is September 24, 2007.

Hilary Cornell made a motion to approve. Carol Stukes seconded the motion.

The motion to approve carried unanimously 7-0.

Case of Anthony DiPatri, Application for Service-Connected Disability Benefits – Plan "B"

This is an application by Anthony DiPatri, former Police Officer, Police Department, for Service-Connected Disability Benefits in Plan "B".

Mr. DiPatri sustained the injury while working when he fell off of his bicycle and injured his shoulder and forearm. His date of injury is October 16, 2007.

Celia O'Leary made a motion to approve. Carol Stukes seconded the motion.

The motion to approve carried unanimously 7-0.

Case of Michael Johncola, Application for Service-Connected Disability Benefits – Plan "B"

This is an application by Michael Johncola, former Police Officer, Police Department, for Service-Connected Disability Benefits in Plan "B".

Mr. Johncola sustained the injury while working when he was struck in the rear of his motorcycle. He was ejected from the motorcycle and thrown 30 feet. In the second incident, he was in a marked car and his car was struck by another vehicle.

The nature of Mr. Johncola's disability is a brain injury. The dates of his injuries are August 15, 2006 and November 13, 2009.

Carol Stukes made a motion to approve. Veronica Pankey seconded the motion.

The motion to approve carried unanimously 7-0.

<u>Case of Tonia Rice, Application for Service-Connected Disability Benefits – Plan "B"</u>

This is an application by Tonia Rice, former Police Officer, Police Department, for Service-Connected Disability Benefits in Plan "B".

Ms. Rice sustained the injury when a case that she attempted to place in her registered patrol vehicle, weighing approximately 30-40 pounds, fell on her right hand and wrist.

The nature of Ms. Rice's disability is limited mobility due to extreme pain and swelling in right wrist and hand. Her date of injury is June 2, 2008.

Carol Stukes made a motion to approve. Veronica Pankey seconded the motion.

The motion to approve carried unanimously 7-0.

<u>Case of Willie Furtick, Application for Service-Connected Disability Benefits – Plan "J"</u>

This is an "***administrative application***" on behalf of Willie Furtick, former Equipment Operator I, Streets Department, for Service-Connected Disability Benefits in Plan "J".

Mr. Furtick sustained an injury when he fell out of his trash truck and fell and injured his knee. His date of injury is March 4, 2005.

Hilary Cornell made a motion to deny. Brian Albert seconded the motion.

The motion to deny carried unanimously 7-0.

OLD BUSINESS

Case of Joseph A. Veneziale, Request to Withdraw Contributions, Plan "B"

This case was **denied** at the October 27, 2011 Board Meeting. A Hearing Panel was held on January 11, 2012.

The Hearing Panel votes are as follows:

Mr. Harvey Rice:	Recommend denial.
Ms. Carol Stukes:	Recommend denial. Employee has already received his contributions. Additionally, employee was afforded the opportunity to receive his contributions in 2009.
Ms. Paula Weiss:	Recommend denial. Option chosen at time of retirement is irrevocable.

The history of the case is as follows:

This is a request by retiree Joseph A. Veneziale, to withdraw his pension contributions in order to pay legal fees and court ordered spousal support.

Mr. Veneziale retired October 6, 2009 and selected survivorship option #4 naming his wife as survivor.

In his letter dated August 18, 2011, Mr. Veneziale states his wife was involved in an auto accident which has caused irreconcilable issues in their marriage. Mr. Veneziale further states his son attends private school and he has a mortgage.

On August 22, 2011, Mr. Veneziale's request to withdraw his pension contributions was administratively denied by Shamika Taliaferro, Program Pension Administrator per Section 22-306(4) of the Code which states election of survivorship option is irrevocable.

Mr. Veneziale is appealing the administrative denial of his request to withdraw from his pension contributions.

Brian Albert made a motion to deny. Hilary Cornell seconded the motion.

The motion to deny carried 6-0-1.

NEW BUSINESS

William Buck – Reinstatement of Pension Benefits

William Buck was approved at the September 27, 2011 Board meeting for Pension Disqualification. He appealed that decision and on January 12, 2012, a hearing panel was convened. At the hearing, Mr. Buck provided documentation which indicated that he was not on duty at the time of the activities which led to his arrest. In light of the evidence and testimony presented by Mr. Buck at the hearing, it is the opinion of the Law Department that pension disqualification is not appropriate, and the Board should vote to grant the appeal of William Buck, which would reinstate him as a member of the City's retirement system.

Carol Stukes made a motion to approve the reinstatement of Mr. Buck's pension benefits. Veronica Pankey seconded the motion.

The motion to approve reinstatement of William Buck's pension benefits carried unanimously 7-0.

Executive Director's Report - Mr. Bielli stated that the Dawn Pettus case which has been tabled for several months will be placed back on the Agenda in March. The Trustee Election Request for Proposal (RFP) went out on February 22, 2012 with a reply date of March 13, 2012. This will allow time for the responses to be reviewed. Prior companies that were used were notified in addition to other companies that may be interested.

On behalf of the trustees who attended the NCPERS Legislative Conference in February, John Reilly submitted materials received at the conference. The materials will be copied and sent to the Board members.

Litigation Summary – Mr. DiFusco stated that the Valerie Rodgers-Rice decision was overturned in Common Pleas Court. The Law Department does not expect to file an appeal. The DiLacqua decision was also overturned by Judge Tucker. There wasn't an opinion with the decision so the Law Department is still reviewing whether or not it will be appealed to Commonwealth Court. Three cases, Spellman, Timcho and Vaughan were affirmed in Common Pleas Court and Russell Ferrante filed an appeal.

Alan Butkovitz joined the meeting at this point.

Cheiron Consulting – Preliminary Actuarial Valuation Report

Ken Kent introduced himself, Karen Zangara and Anu Patel who would be presenting that day. He stated the presentation will include an overview of the year, historical review, preliminary 7/1/11 valuation results, stress testing and other items that impact results.

He started by saying it was a good year. The market return was on average 19.4% and it produced a 19.9% actuarial asset return which is also favorable and the net impact of that is $84,000,000 more in the fund than was anticipated. What is more significant is that the ratio of actuarial to market asset value is 110.8% versus 127.1% last year before application of corridor significantly reducing the amount of unrecognized losses.

Active participants decreased 4.5% from last year to this year (June 30) and total payroll salary decreased 3.5%, resulting in a 1% increase in salaries of the participants, which produced an overall gain in the fund of $54,000,000.

Two changes were made in assumptions: (1) they assumed the Police Plan 87 participants would elect Option 4 at retirement; and (2) that pension benefits are paid at the end of the month. The net impact of this was a decrease in liabilities of $59,000,000. The Option 4 assumption increased liabilities by about $25,000,000 and the timing decreased liabilities by about $80,000,000. The net results show that the ratio of assets to liabilities increased from 47.0% to 50.0% from 2010 to 2011.

Anu Patel presented the historical review of the assets and liabilities, the funding policy/MMO, MMO contributions by source, participation and annual cash flows. There is a two year lag in calculation of the MMO so the most recent valuation done was for 2011. July 1, 2011 is used for the calculation of the MMO as of Fiscal Year ending 2013.

Mr. Kent added that 2013 reflects when the City begins to pay off the maturity of the deferred contribution component that is built into the MMO.

Mr. Reilly asked if that is repayment of the $150,000,000 and $80,000,000.

Mr. Dubow stated that 2011 and 2012 have deferrals and the interest on the deferrals starts in 2011 and continues in 2012. Then the interest and principal gets repaid in 2013 and 2014.

Mr. Butkovitz asked when we will have realized the end point of the 5 year re-amortization bubble, and if that line is extended to 2015 will there be a declining number in terms of percentage of payroll.

Mr. Kent answered that Fiscal year 2014 is when that gets paid off.

Anu Patel explained the demographic chart which shows the active population, DROP, vested, and retirees. The top of the chart shows the ratio from active to inactive which is a measure of the maturity of the Plan. There is a ratio of .8 active employees for every retiree.

Mr. Dubow asked how that compares to other Plans, and if it is a high, low or average ratio.

Mr. Kent stated that for mature systems it's about right, when you look at the cost of the system as a percent of payroll. When you lose a dollar of income, that's a dollar of retiree liability and assets and it's a dollar of active assets, but as a percent of the payroll its paid back on the active lives only so it's a kind of leverage that says for every dollar we lose for retirees and actives it means two dollars on active payroll. If you're benchmarking how much the system costs as a percent of payroll and looking at 34%, part of it is a function that you only have less than one active for each retiree. If you had five actives for each retiree, the loss you experienced would not be as significant. If you look at the cost of the system for the 67 Plans where the ratio is much lower actives to retirees you'll see the costs are well above 100%, which you expect for a closed tier. Ultimately, the costs would be infinite when there are no more actives in those plans. It is a mature plan, we are developing this leverage ratio index and working with Boston College and their database and it defines how much the multiples of how much your unfunded is to your payroll, compares it to a national database, to measure the relative risk of your system. It can help you make decisions how you invest the funds and manage volatility.

Mr. Leonard asked how the ratio changes as it continues to age beyond 2011.

Mr. Kent said the ratio has remained relatively constant for the past 15 to 20 years. It has been declining a little because of the decline in the active population but it has always been 50/50, 30,000 retirees and 30,000 employees. Some of the steps the City has taken is how many employees the City is employing and the number is going down. Another thing that is probably affecting this at the same time is the influx of DROP participants who are counted as retirees.

Ms. Patel explained the chart on the annual cash flows, the contributions that come into the Plan and the benefits and expenses that are paid out. The net cash flow has been negative throughout the period. It has been steady between 2007 and 2010 and for the first time there has been a decrease in the net cash flow and mostly because the contribution at year end increased.

Ms. Stukes asked if all the numbers mean that the Fund has increased.

Mr. Dubow said the answer is no.

Mr. Kent explained that the dependence of these numbers on the assets is a function of the impact on contribution. The benefit payments are obviously known on a historic basis. The Plan is paying out more in benefits than contributions. The positive aspect of higher contributions which are a function of the investment market, is that the contributions are getting closer to the amount being paid out in benefits. That means the net additional cash that is needed to pay out benefits over and above the cash received in contributions is getting smaller. What is the negative cash flow as a percent of pay is the hurdle. You have to make that percent first before you can anticipate that assets will grow from year to year. If more contributions are put in the hurdle rate will be smaller. The funding ratio will grow at a very slow rate unless there's some extraordinary events like the market return at the end of 2011.

Mr. Stagliano said they could lower the assumed rate of return.

Mr. Kent said by virtue of increasing contributions it solves negative cash flow problems

Mr. Leonard asked what the hurdle rate for 2011 is.

Mr. Kent said it's about 2%. The benefit payments grew a little bit and the contributions grew significantly.

Anu Patel explained the summary of participation from July 1, 2010 to July 1, 2011. The active population decreased 4.5%. The retirees were level, beneficiaries decreased slightly and terminated vested decreased 17%. The total payroll decreased about 3.5 % and the average salary for the active population went up 1%, which was lower than the assumption. The average monthly payment to retirees and beneficiaries went up 2.7%.

Mr. Butkovitz asked what the assumption was for the active population. If it's 1% instead of 3.5%, the unions contributed substantially to the health of the pension fund.

Ms. Zangara explained they have a graded scale now. In terms of payroll growth it is based on the years of service so it ranges from an increase of 2% to 10% based upon the assumptions someone has worked for the City. The financial experience on the market return on assets was 19.44% which was above the expected return. The actuarial value of assets is smooth assets and has increased to 9.93%. The smooth assets decrease the unfunded liability. The expected market value return was 8.15%. On the historical market value returns we are now in positive territory for the three year average at 4.46%. The 5 year average and 10 year average are at 5.17% and 5.96%. The Pension Adjustment Fund increased slightly and there was no transfer into the path this year. The DROP accounts increased to 4%.

Ms. Zangara explained how the smooth actuarial value of assets is calculated, the Pension Adjustment Fund and the Liability Experience. The liabilities were lower than expected because of salaries and the decrease in the active population, but it was offset by people moving from actives to DROPS or retirement status. There was a decline in the payroll which caused a decrease in the normal cost, which is the accrued amount for the year which decreases the MMO for the year. There was an increase in the actuarial value of assets due to market gain and the funding ratio increased from 47% to 50%. The projected MMO is lower than estimates by about 4.5%.

Ms. Zangara presented on the key valuation results. The present value of future benefits are the accrued liability to date plus the additional piece the actives would get if they continue to work. That has gone up from 10.3 billion to 10.4 billion. When they look at the total, current and future resources and break it down by current and future resources, the present value of future employee contributions, normal costs, market value of assets, and present value of future amortization payments. That went down. When you add everything up the deficit went down from $730,000,000 to $459,000,000 million. The contributor there was the market value of assets.

Mr. Leonard asked what discount rate is used.

Ms. Zangara said the discount rate is 8.15. The actuarial liabilities did go up and there were gains for the actuary liabilities but less than anticipated, that's why there is a gain.

Mr. Butkovitz asked how this would have been forecast a year ago.

Mr. Kent replied that the actuarial liability would have been about 9.5. Last year at this time they were not projecting the funding ratio to be above 50%. There was a discussion at the last year's meeting about when that might happen. The actuarial value of assets would have been 4.4 billion and the liability close to 9.5 billion.

Mr. Butkovitz said this strikes him as kind of an outlier in terms of forseeability, as this is a dramatic change in conditions in one year. This demonstrates that there is an upside to the possibilities here that is beyond what is routinely forecast on these charts.

Mr. Kent said there are two components here, one is the fiscal structure which has a lower payroll growth and fewer active participants, 19% return is an outlier, at a 8% return the level of risks might be around 11%, that says there a 66% chance the returns will be somewhere between positive 19% and negative 3% so you're within that realm.

Mr. Butkovitz commented that this is a rebuttal to the Northwestern actuaries who predicted doomsday for the Fund and defined benefit plan. It is not doomsday for the Philadelphia Pension Fund and we have to thank the Mayor also for policies, in addition to the Unions. Things have worked out well in the past year. Both the Mayor and the Unions should be thanked for their contributions.

Ms. Stukes said that's why the Board didn't hire Northwestern because they had the foresight to know they didn't know what they were talking about. They picked good managers and had good people in place to get to where they are now. She gives everyone around the table credit but will not go as far to give the Mayor anything when her people have been sitting out here for five years without a contract and he took everything from them such as step increases and no pay raises.

Mr. Butkovitz stated that the point is that the conventional thinking is we have to rip up everyone's pension because we're heading off a cliff and it's not reality, you read about that stuff when somebody comes up with some crazy analysis based on phony figures so now you have real figures. All the experts want to weight in and change things dramatically without knowing what they're talking about. They need to be confronted with the real numbers now that the actuarial report is available. PICA wants to reconsider what the pension should be in Philadelphia because they say it's not solvent, but that's not the truth and an event has happened that is newsworthy.

Mr. Reilly stated the report that Mr. Butkovitz is talking about was written by a professor who received his figures from the Mayor.

Mr. Butkovitz said this improvement should be highlighted in evaluation.

Mr. Dubow commented they should be careful because we are still only 50% funded and we don't want to go overboard.

Mr. Kent said that going forward, that is correct, if they got retroactive raises that would have an impact in terms of the creation of additional unanticipated liability.

Mr. Kent said that $680,000,000 is your hurdle rate in terms of contribution level. To get your hurdle rate to be zero your contributions have to equal your benefit payments.

Mr. Butkovitz asked if the variable was the return on investments, what the return would have to be.

Mr. Kent stated that if you have a negative cash flow that difference comes out of the return, if your negative cash flow is -2% you need to get a 2% return to cover the negative cash flow before you expect the at market value assets to grow.

Mr. Butkovitz asked if you achieve a certain rate of return then you'll be able to make the payments without increasing the contribution rate. What rate of return would you need to make.

Mr. Kent answered you would need to make 8.15% each and every year then the contribution rate would have to be higher, you still have investment loss being spread out six years. He stated he could it explain it better when they get to the model.

Mr. Kent explained the components of the MMO for the Fiscal Year ending 2013 and the gain and loss summary for the year. This answers the questions about where you would have been if everything was as expected. We would have expected the liabilities to grow by the normal cost, and be offset by the benefit payments. The expected interest if we got the 8.15 % would have added $742, 000,000, so we would have expected our liabilities to be just under 9.5 billion dollars. On the asset side, instead of the normal cost we look at the total contributions, quasi and member contributions and deferred contributions which according to the law we are recognizing it as it has been paid in decreased by the same benefit payments.

Mr. Kent explained the chart on the funding policy and the contribution rate and finished the presentation with stress testing for the future.

There was discussion on reducing the assumption rate. The projections are still below what the City used in their most recent Plan. Mr. Dubow asked what rate would get us to the numbers that Mr. Kent gave them in December when they were preparing their plan.

Mr. Kent stated that if the rate was 8.1% that would almost be a break-even of what the City's plan is which would mean you could reduce the assumption by 5 basis points and still fall within that rank as of June 30, 2011. The value of discussing the reduction of the rate is that every time you reduce the rate you reduce the risk of failing to meet that rate. It makes it easier to meet your expectations.

Mr. Butkovitz asked what accumulated gains and losses are currently being amortized.
Mr. Kent replied when you get the report you'll have a table of each of those pieces. It started in 2009 and you're looking at gains and losses in 2010 and 2011. This year will be

$160,000,000 of gain that you're amortizing. There is a huge unfunded amortization base which takes into account all the past accumulated gains, losses, assumption and benefit changes.

Mr. Butkovitz asked if the losses are being divided by 15 years or only the gains.

Mr. Kent said they are determining the losses and gains and coming up with a net number and amortizing it over 15 years.

Discussion continued about the assumed rate of return. Mr. Kent stated that nationally, 8% is probably the most predominately used rate and most systems are reducing their rate.

Alan Butkovitz made a motion to change the actuarial assumed rate of return to 8.1% for Fiscal Year July 1, 2011 – June 30, 2012. Ronald Stagliano seconded the motion.

The motion to change the actuarial assumed rate of return to 8.1% for Fiscal year July 1, 2011 – June 30, 2012 carried unanimously 8-0.

Brian Albert made a motion to adjourn. Ronald Stagliano seconded the motion. The meeting adjourned at 11:00 a.m.