



MINUTES

BOARD OF TRUSTEES

OF THE TEACHERS' AND STATE EMPLOYEES' RETIREMENT SYSTEM

The regular quarterly meeting of the Board of Trustees was called to order at 9:30 a.m., October 26, 2017, by the Chair, State Treasurer Dale R. Folwell, CPA. The meeting was held in the Dogwood Conference Room of the Longleaf Building at 3200 Atlantic Avenue, Raleigh, NC 27604. The Chair informed that there would be a public comment period for organizations and individuals to address the Board.

Members Present

The Board members present were: Treasurer Dale R. Folwell, Lentz Brewer, Barbara Gibson, Greg Grantham, Michael Mebane, Claire Miller (on behalf of Superintendent Mark Johnson), Greg Patterson, Margaret Reader, Joshua Smith and Jeffrey Winstead.

Members Absent

The absent board member was Van Dowdy.

Guests Present

The guests attending were: Jody Newsome from the Attorney General's Office and Michael Ribble and David Driscoll from Conduent Consultants.

Department of State Treasurer Staff Present

The staff members present were: Steve Toole, Thomas Causey, Chris Farr, Joan Fontes, Jaclyn Goldsmith, Sam Hayes, Matthew Krimm, Fran Lawrence, Karah Manning, Lisa Norris, Vicki Roberts, Laura Rowe, David Starling, Edgar Starnes, Christina Strickland and Sam Watts.

Ethics Awareness and Identification of Conflicts or Potential Conflicts of Interest

The Chair asked, pursuant to the ethics rules, about conflicts of interest of board members. No conflicts of interest were identified by the board members.

Approval of the Minutes from the July 20, 2017 Board Meeting

It was moved by Greg Patterson, seconded by Greg Grantham, and carried unanimously by the Board that the minutes from the Board meeting held on July 20, 2017, be approved.

Retirement Systems Division Operations

The Chair recognized Thomas Causey, Deputy Director of Operations, and Vicki Roberts, Deputy Director of Member Services, for an update on Retirement Systems Division operations. Mr. Causey gave a report on the metrics for operations and Ms. Roberts gave an update on the metrics for Member Services.

Mr. Causey gave a report on overpayments, stating that \$10.9 million has been collected over the past 13 months. He commented that the department has been working with the Department of Revenue to intercept the state tax refunds and lottery winnings of members with outstanding

overpayments. Mr. Causey also reported that 120 retirements have required an additional employer contribution pursuant to the Contribution-Based Benefit Cap as of October 4, 2017. The department has sent invoices totaling \$11.1 million, and 94 employers have paid in full.

Investment Advisory Committee (IAC) Update

The Chair recognized Greg Patterson for an update on the IAC meetings. Mr. Patterson stated to the Board that annual cost-efficiencies for the North Carolina Retirement Systems investment program have increased from \$50 million to \$62 million. He stated that the market value of funds has reached \$94 billion for the North Carolina Retirement Systems. Mr. Patterson shared the current focus of the IAC, Investment Management Division and the Department of State Treasurer is asset allocation of the portfolio. Mr. Patterson reviewed the portfolios and stated that, due to historical manually tracking, this is the first year that the 20-year portfolio investment return is available. He stated that the North Carolina Retirement Systems earned 6.7 percent as of June 30, 2017 over a 20-year annualized period. He compared the returns to the long-term policy benchmark that earned 6.1 percent and the implemented benchmark (consisting of 18 benchmarked peers with assets of \$20 billion and over). Mr. Patterson stated that the North Carolina Retirement Systems portfolio return was below the assumed rate of return of 7.2 percent for years three, 10 and 15; however, the portfolio achieved higher return than assumed during years one and five. Mr. Patterson stated that the risk ranking for the North Carolina Retirement Systems was lower compared to other public funds over \$20 billion. Lastly, Mr. Patterson also stated that total Department of State Treasurer assets under management is at \$123.2 billion as of June 30, 2017.

Presentation on the Decennial Rules Pursuant to N.C.G.S. §150B-21.3A

The Chair recognized Christina Strickland, General Counsel for the Retirement Systems Division, for a presentation on the Decennial Rules Review. Ms. Strickland explained that N.C.G.S. §150B-21.3A established a process and schedule for agencies to decennially review their active rules codified in the North Carolina Administrative Code (NCAC) with oversight by the Rules Review Commission (RRC). She stated the requirement in the Administrative Procedure Act for agencies to review their rules to determine whether each rule is unnecessary, necessary with substantive public interest or necessary without substantive public interest. When a rule is classified an unnecessary, the Codifier of Rules will remove the rule from the NCAC without any further action by the agency. Ms. Strickland detailed the process for reviewing existing rules as described in N.C.G.S. §150B-21.3A(1)-(3), and presented the proposed initial rule classification determinations for the existing rules. Lastly, Ms. Strickland informed the Boards that Session Law 2015-164 (Retirement Administrative Changes Act of 2015) amended the Administrative Procedure Act by adding N.C.G.S. §150B-21.3A(e)(1) which creates an exception for rules deemed by the Boards of Trustees of the Retirement Systems to protect inchoate or accrued rights of retirement system members. The provision states that these rules will not expire.

It was motioned by Lentz Brewer, seconded by Margaret Reader, and carried unanimously by the Board to make the determinations classifying each rule in the Decennial Rules Review Initial Report and to authorize the Department of State Treasurer staff to take all additional necessary steps required to complete the Decennial Rules Review process, in accordance with N.C.G.S. §150B-21.3A, as well as, to make the determination that the rules in the Retirement Inchoate Rules Report protect inchoate or accrued rights of the retirement members in accordance with N.C.G.S. §150B-21.3A(e1).

Retiree Health Benefit Fund Staff Offsets to Retirement Administrative Budget (1410 Retirement Operations)

Steve Toole, Executive Director, presented how Section 2(n) of Session Law 2017-129 amends N.C.G.S. 135-7(f) to provide, in pertinent part:

It is the intent of the General Assembly that the Retiree Health Benefit Fund (RHBF) be a trust that provides an irrevocable source of funding to be used, to the extent the assets are sufficient, only for health benefits to retired and disabled employees and their applicable beneficiaries.

The RHBF assets may be used for reasonable expenses to administer these health benefits, as approved by the Board of Trustees, including offsets to the state budget to the Retirement Systems Division for staff administration and benefits.

Executive Director Toole recommended that the Board of Trustees approve the establishment of the three positions for the purpose of administering the benefits provided by the RHBF, consistent with Session Law 2017-129. The three positions are as follows:

Position	Total Salary and Benefits
Administrative Support Specialist (Lead)	\$57,822
Administrative Support Specialist	\$52,083
Administrative Support Specialist	\$52,083

It was moved by Greg Patterson to approve the establishment of the three positions for the purpose of administering the benefits provided by the RHBF, which would allow RSD to offset the budget for staff administration of benefits of the positions that have already been allocated to the RHBF. Greg Grantham seconded the motion, and it carried unanimously by the Board.

Closed Session Pursuant to N.C.G.S. §143-318.11(a)(3)

The Chair asked for a motion to enter into closed session pursuant to N.C.G.S. §143-318.11(a)(3) to consult with legal counsel regarding pending litigation involving Johnston, Wilkes, Union and Cabarrus Counties Boards of Education. It was moved by Michael Mebane, seconded by Claire Miller, and carried unanimously by the Board to enter into closed session. All attendees, other than the Board members and applicable staff, were instructed to exit the conference room.

Greg Patterson made a motion to reopen the meeting, which was seconded by Lentz Brewer and carried unanimously by the Board.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2016, by Conduent for TSERS

The Chair recognized David Driscoll and Michael Ribble, from Conduent HR Solutions, for a presentation on the findings on the TSERS actuarial valuation. The actuaries reviewed the membership data for TSERS, stating that the active membership decreased by 0.01 percent and the retired members and survivors increased by 3.4 percent. They reported that compensation has increased by 2.7 percent (compared to the three percent anticipated) and that payroll has slightly grown over the past five years. They reported that as of December 31, 2016, the market value of assets was at \$64.2 billion, an increase from the 62.7 billion at 2015 year end. They reported that the estimated net investment return on market value was 6.22 percent in this valuation. Because the returns were below the assumed rate of return of 7.25 percent for calendar year 2016, this deviation results in a higher required contribution than anticipated as of the December 31, 2016 baseline projections presented in the December 31, 2015 actuarial report. The actuaries reported that based on historical market returns, current asset allocation, current investment policy and the expectation of future asset returns, as reviewed by the last experience study, the 7.20 percent discount rate used in the valuation was reasonable and appropriate.

The actuaries reviewed the legislation signed into law since the prior valuation that impacts benefits, stating that the one percent cost-of-living-adjustment (COLA) was made effective July 1, 2017, for retired members and survivors of deceased members receiving benefits as of July 1, 2016. Additionally, a reclassification for probation/parole officers to convert to service rendered similar to law enforcement officers on or after July 1, 2017. There was discussion by the Board on the abilities to grant COLAs.

The actuaries discussed the actuarial assumptions in regards to demographic and economic assumptions, the funding methodology in regards to actuarial cost methods, and valuation and amortization models. They presented the actuarial value of assets, stating that the market value of assets is lower than the actuarial value of assets, which is used to determine employer contributions. This difference will result in unrecognized losses that occurred through 2015 that will be smoothed out through the next five years. There was Board discussion around the ability to meet the required return over a 10-year period. Mr. Ribble discussed the actuarial accrued liability in comparison to the actuarial value of assets and reported that the funded ratio for TSERS decreased from 92.5 percent from the December 31, 2015 valuation to 90.4 percent for the December 31, 2016 valuation.

Mr. Driscoll and Mr. Ribble reviewed the Employer Contribution Rate Stabilization Policy (ECRSP) and presented that the Actuarially Determined Employer Contribution (ADEC) would be 11.98 percent of payroll for fiscal year ending 2019 (based on last year's final rate of 10.53 percent in addition to 0.45 percent for two legislative changes and the 0.35 percent increase under the ECRSP).

Based on actuarial losses recognized in the December 31, 2016 valuation, no COLA could be funded by actuarial gains during the 2018 year. Additionally, the valuation presentation included information that detailed fiscal circumstances needed in order to produce the required investment gains to warrant a COLA. Based on the methods and assumptions used for the projections, Conduent estimates that a potential COLA effective July 1, 2019, may be funded by actuarial investment gains following the December 31, 2017, valuation in the following circumstances:

- If calendar year 2017 market value returns exceed 16.9 percent, the plan is estimated to have an actuarial investment gain for 2017 and a COLA that would take effect on July 1, 2019, could be considered
- If calendar year 2017 market value returns exceed 20.7 percent, the plan is estimated to have an actuarial investment gain for 2017 and such gain may be enough to consider providing a one percent COLA that would take effect on July 1, 2019

Mr. Driscoll and Mr. Ribble discussed the funded ratio alternatively based on the 30-year treasury rate that is to be required in the actuarial valuation as required by Session Law 2016-108. They reported that based on the current 30-year treasury rate of 3.06 percent, the funded ratio would be 52.7 percent.

Lastly, Mr. Driscoll and Mr. Ribble gave a presentation on the baseline projections based on December 31, 2016, valuation results and required investment return of 7.20 percent. They alternatively demonstrated projections under a 0 percent and 14.4 percent return for all years.

It was moved by Lentz Brewer, seconded by Joshua Smith, and carried unanimously that the actuarial valuation for TSERS as of December 31, 2016, be accepted.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2016, by Conduent for the Consolidated Judicial Retirement System (CJRS)

Mr. Driscoll and Mr. Ribble presented the findings of the CJRS actuarial valuation. The actuaries reported on the key takeaways of the valuation, stating that the market value return was 6.22 percent, compared to 7.25 percent return assumption; and there was an increase in payroll of 2.7 percent, compared to the three percent expected increase. The actuaries reviewed the one percent COLA that was made effective July 1, 2017, for retired members and survivors of deceased members receiving benefits as of July 1, 2016, (and prorated increase for those retired after July 1, 2016 but before June 30, 2017). Lastly, Mr. Driscoll and Mr. Ribble reviewed that the change in discount rate of 7.25 percent to 7.20 percent was made effective as of December 31, 2016.

Mr. Driscoll and Mr. Ribble reported to the Board that the December 31, 2016, valuation yielded a lower funded ratio of 87.9 percent (compared to the December 31, 2015, valuation that resulted in an 89.4 percent funded ratio). This deviation results in a higher actuarially determined employer contribution rate of 32.35 percent for fiscal year ending June 30, 2019, (compared to 30.23 percent calculated for fiscal year ending June 30, 2018).

It was moved by Michael Mebane, seconded by Lentz Brewer, and carried unanimously by the Board that the actuarial valuation for CJRS, as of December 31, 2016, be approved.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2016, by Conduent for the Legislative Retirement System (LRS)

Mr. Driscoll and Mr. Ribble presented the findings of the LRS actuarial valuation. The actuaries reported on key takeaways from the valuation, stating that: the market value return was 6.13 percent, compared to the 7.25 percent required return; the decrease in payroll of one percent, compared to approximately three percent expected. The actuaries reviewed the one percent COLA that was made effective July 1, 2017, for retired members and survivors of deceased members receiving benefits as of July 1, 2016, (and prorated increase for those retired after but before June 30, 2017). Lastly, Mr. Driscoll and Mr. Ribble reviewed that the change in discount rate of 7.25 percent to 7.20 was made effective as of December 31, 2016.

Mr. Driscoll and Mr. Ribble reported to the Board that the December 31, 2016 valuation yielded a lower funded ratio of 95.9 percent (compared to the December 31, 2015 valuation that resulted in a 99.0 percent funded ratio). This deviation results in a higher actuarially determined employer contribution rate of 21.74 percent for fiscal year ending June 30, 2019, (compared to 18.27 percent calculated for fiscal year ending June 30, 2018).

It was moved by Lentz Brewer, seconded by Greg Patterson, and carried unanimously by the Board that the actuarial valuation for LRS, as of December 31, 2016, be approved.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2016, by Conduent for the Disability Income Plan of North Carolina (DIPNC)

Mr. Driscoll and Mr. Ribble gave a presentation on the principal results of actuarial valuations, as of December 31, 2016, for DIPNC. The actuaries reported that active membership decreased slightly since the 2015 valuation, and there was an increase in the surplus of assets of 128,724,997 (increase from 124,262,665 from the December 31, 2015, valuation). Mr. Driscoll and Mr. Ribble reported that the preliminary-determined actuarial required contribution (ARC) is 0.13 percent for fiscal year ending June 30, 2019 (a decrease from 0.14 percent for fiscal year ending June 30, 2018).

It was moved by Margaret Reader, seconded by Lentz Brewer, and carried unanimously by the Board that the actuarial valuation for DIPNC, as of December 31, 2016, be approved.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2016, by Conduent for the National Guard Pension Fund

Mr. Driscoll and Mr. Ribble presented the findings of the National Guard Pension Fund actuarial valuation. The actuaries reported that the valuation results yielded a funded ratio of 68.6 percent (an increase from 67.0 percent from the December 31, 2015, valuation). The actuaries explained that due to recent history of benefit increases, the funded status of the National Guard Pension Fund is lower than the other NC Retirement System Plans. As a result of the unfunded liabilities the plan has undertaken, less than five percent of the ADEC is going towards the cost of service to be paid while service is accruing, and that more than 95 percent of the ADEC pays for pension debt. Mr. Driscoll and Mr. Ribble reported that the ADEC for the National Guard Pension Fund will be \$9,071,933 for fiscal year ending June 30, 2019, (an increase from \$8,923,153 for fiscal year ending June 30, 2018).

It was moved by Greg Grantham, seconded by Lentz Brewer, and carried unanimously by the Board that the actuarial valuation for National Guard Pension Fund, as of December 31, 2016, be approved.

Presentation by the Consulting Actuary on the Principal Results of Actuarial Valuations, as of December 31, 2016, by Conduent for the Death Benefit Plans

Mr. Driscoll and Mr. Ribble presented the findings of the Death Benefit Plans actuarial valuation. The actuaries reported that the Death Benefit Plan for TSERS has a surplus of \$92.7 million and a set contribution rate of 0.16 percent. Mr. Ribble reported that the current assets and contribution rates of the Retirees' Contributory Death Benefit Plan are not adequate to address the \$47.4 million gap between assets and liabilities. They reviewed the Boards' decision in April 2016 to increase the premiums for members who retire March 1, 2017, or later, which will lessen future growth of the deficit for future retirees; and, decreasing the interest paid on return of contributions to 1.2 percent, which would be applicable to retirees whose death occurs prior to 24 months of coverage. The actuaries reported that according to GASB 74 payout projections, the assets of the Retirees' Contributory Death Benefit Plan are projected to be exhausted by 2070.

It was moved by Greg Grantham, seconded by Greg Patterson, and carried unanimously by the Board that the actuarial valuation for TSERS Death Benefit Plans, as of December 31, 2016, be approved.

Public Comment Period

The Chair recognized the following organizations' representatives for presentations on retirement benefit proposals for the Board to consider:

- Margaret Foreman, representative from N.C. Association of Educators, gave a presentation on the need for a legislative appointment of the active and retired teacher positions on the Board and requested the Board's consideration in the support of filling any vacant positions that are appointed to represent North Carolina teachers.
- Richard Rogers, representative from N.C. Retired Government Employees' Association, gave a presentation on the COLA needs of local government retirees and requested the Board thoughtfully consider the need of a LGERS COLA during the coming fiscal year.

State System Adjournment

There being no further business before the Board, Lentz Brewer moved to adjourn, which was seconded by Greg Patterson, and the meeting was adjourned unanimously at 12:25 p.m.

Chair

Secretary