June 26, 2012
SPECIAL MEETING PENSION PLAN B

The Board of Trustees, Pension Plan B, met on the above date.

President Rosenberg called the meeting to order at 6:00 p.m.

Present: President Rosenberg, Treasurer Morley,
Trustees Buck, Herlihy, Klein, Lee, Meszoros and Rodriguez

Tom Dawidowicz, The Segal Company
Attorney John Galiette, Reid and Riege
Timothy Ryor, Hooker & Holcomb
David Reiser, Morgan Stanley, Smith Barney
Mark T. Anastasi, City Attorney

Absent: Vice President Ana Garcia and Trustee Doris G. Garcia

Old Business:

1. None.

New Business:

1. Presentation of Report by Hooker and Holcomb.

Consulting Actuary Timothy Ryor
I will go through the report page by page and feel free to ask questions as we go along. The purpose of the project was to calculate the liabilities of the retirees not being transferred to MERS. We were told that the trustees wanted to use the ERISA standard as a starting place.

The first order of business for us was to value the plan. We got data from Segal. We were able to match their liabilities very closely. We got within a comfort level and we felt that we understood the plan and we were following the same methodology that Segal was using.

Turning to page 2, we give you the back ground; we talk about the ERISA standard. The purpose of the rules in ERISA is to give a base line for if you are splitting a plan apart and you are subject to those rules, the goal of those rules are to provide two plans that are as well funded under those rules as they were aggregated together.

Page 7 goes through the different categories and the allocation. Category 3, it relates to liabilities contributable to people in pay status as of three years ago, obviously most of that liability is the piece that's staying because those are the people that are staying, those are the people that are currently in pay status. Pay status means the retirees. Category 4, it's essentially the rest of the liability. Category 5 is the non vested liability, those would be the people that wouldn't have had 5 years of service.

We were reporting an asset value and obviously this isn't the official June 30, it's an estimate thereof, it's 72.56 million, 57 million. When you allocate it based on the categories, you're going to do a spin off, the bottom line you would get this split you would leave 53.7 million behind and transfer 18.8 million to the spinoff plan. That was the starting point. We talk about this in the commentary, why this may or may not be appropriate. The purpose of this kind of split subject to ERISA is to make sure that on this category basis the two resulting plans would be equally well funded on a termination basis according to the categories.

For starters, your plan is not covered by ERISA and also you're spinning off into an entity that really doesn't require, that's already funded, it's an existing plan, so really the conditions are different. So, we took a look at it from another standpoint, what is it that you need left in the plan to satisfy certain criteria. To be confident that there is enough money that can be conservatively invested without taking undue risk and you can be confident that that money will be there and no additional contributions will need to be put into the fund. On page 1, that's really Scenario 4. What we did was we said what is that long term investment return. Obviously, this is just retirees; they are a small portion of the liability. So you have a fairly short duration liability that's in pay status, there's no money expected to come in between employee or employer contributions, so what would that rate be. We look at the bond market, we look at the capital market expectations with your investment advisors and came up with a net investment return of 4 ¼ per cent. That's the number that's calculated on page 4. When you look at it that way what the fund would need is 50.915 million dollars to basically be confident that the payment stream for those remaining individuals, there is a summary of the data and the people we are talking about and the benefit levels on page 8. Related to the assumed payment it's very important to recognize as you know, the plan has a COLA. We used the same assumption that Segal used in their valuations which is 3%. If you go to page 6 we actually kind of give you a range of numbers to give you a sense of both impact of different investment returns and a different COLA assumption so you could get a sense of what the liabilities do if you assume different things related to both COLA and investment return.

At the end of the day our conclusion was that if you are looking to manage this, if the fund will continue and the assets will be managed, but the desire is to lower the risk profile and to have an amount that you believe is secure that you can count on no additional contributions, but there is enough money there that you can earn in a conservative portfolio enough to pay all future benefits including all future COLAS and that's really a big factor because there is some uncertainty related to that COLA, we used that 4.25% net return and arrived at the 50.9 million dollars. That's somewhat less than the 4044 ERISA allocation, but that ERISA allocation assumes a risk free environment. If you wanted the risk free and we do talk about this in the discussion section, if you wanted to take all risk out of this, if you wanted to use the fund to go buy annuities so there was zero risk factor involved the estimate of that liability is the 60.72 million. So that's an important starting point to realize. If we wanted to take all risk out of this, we didn't want to invest the money anymore, we wanted to get out of the pension investment game and just settle this liability as of June 30, one you would need to go to market, this is just an estimate, but assuming that this is a good estimate of market conditions, then you would spend 60.72 million dollars to settle that liability. Now, the lower 50.9 million dollar number, that's assuming that you don't go to market, you invest it yourself, you manage it yourself, you pay the fees to do that, but through that active management you earn, again that 4.25% rate. There's a lot of different ways to attack this. There's no single one right answer. It's just how much can you leave and still be safe and confident that there is enough money in there that you are not going to need more.

Trustee Buck Question to David Reiser
Regarding percentage of 4 1/4%, is that the target percentage to change the asset allocation to an ERISA allocation.

David Reiser
We've already become a little less risky in the portfolio as you know we did that last year. The numbers when we quoted the high end of the range 4.25 that we be comfortable with at that level was based upon making the portfolio less risky than it is even right now.

Treasurer Morley
Response was the 4.25 is 5%. Trustee Buck responded the 5% would be the maximum target.

Trustee Morley Question to David Reiser
How comfortable is Morgan Stanley Smith Barney with achieving consistently the 5% gross return going forward.

David Reiser
We are comfortable with the 4 1/4 net return. Keep in mind that when normal clients come to us without COLAS and ask us what number we're comfortable with giving them an income for the rest of their life without running out of money, we typically quote 4% rate, so we're comfortable with 4 1/4 on the high end range.

Treasurer Morley Question to David Reiser
Now that we are not receiving anymore contributions from either the participants or the City, am I right in assuming that if the market takes a dump, we will really not have any cash to go in and buy up bargains that resulted from the market dump.

David Reiser
That's correct. We use to take advantage of that all the time. We can't do that anymore.

Trustee Buck
Regarding regular employer and employee contributions, those are no longer coming in, however, I believe the plan has not changed, so based upon the actuarial study that's done each year; the City may or may not have a liability. Would that be correct Jim. In other words, the City's expected contribution, if the actuarial study comes in on an annual basis to show that the City has an obligation, they still have that obligation is that correct

Attorney John Galliette
The plan is not subject to ERISA so there isn't a mandatory minimum funding obligation that governmental plans have. There is a contractual obligation, but there isn't something comparable to the ERISA which says every year you have to put a contribution, but ultimately if you set aside a certain amount of assets and it's not sufficient to pay the benefits to the retirees who are left then the City has a contractual obligation to pay those benefits.

City Attorney Mark Anastasi
I had a number of conversations in the last couple of days with Tom Sherwood from OPM and with Segal actuaries, I believe we have Tom Dawidowicz from Segal here and I want to confirm what's being said, and with all due respect is sort of a flawed assumption of the fact that the amount of money that the City proposed along with the MERS people at the State the deposit was insufficient and that's because the City operates on the notion that under Section 13 under the existing agreement the City has a duty based on every three year actuarial studies to deposit not a fixed percentage but whatever is necessary to keep the plan actuarially sound. The plan remains alive for those who are retired. So the goal was to identify an appropriate amount of money that's guestimated or projected by the actuaries to keep the plan actuarially sound at the moment subject to the City's continuing obligation. The problem is that I believe the projection is predicated upon a couple of assumptions or at least one major assumption I heard several times which is you have to look at a fixed amount of money and you have to be concerned that no additional funds are available to the plan and that is absolutely false. I don't think one needs to be quite as cautious or conservative in your projections knowing that there is a fund and an obligation on the City's part to keep the plan actuarially sound just the way it's been going on all along.

President Rosenberg
We had a cash flow situation while Plan B was going. That no longer really is the case. I know what you're saying a contractual agreement, but the people sitting at this table have a fiduciary responsibility. I think everybody here takes it pretty seriously. In light of that, I think that's why we asked to have an independent actuarial study.

Attorney Anastasi
I understand that Mr. Chairman, but with all due respect, the reason why you had a cash flow is because there was a continuing payment obligation. That cash flow is now going to MERS because of the fact that the active employees who continue to contribute will have their appropriate 15% or whatever match coming from the City. That's what it should be.

President Rosenberg
That's good for the people that are moving into MERS, but that may or may not be the case for the people who remain behind.

Attorney Anastasi
If it's not, then the City has an obligation to make a contribution.

President Rosenberg
I understand that and if they do and that's an assumption okay. I know that's why we wanted to have an independent actuarial study.

Attorney Anastasi
I fully understand the theory. The commentary was that the contributions, the City's contributions as you well know always matched the active duty officers. The retirees don't continue to contribute, so that's all I wanted to bring out. If there are questions, we're here to talk, we can talk apart from this room, it doesn't have to be in this form, but Segal was willing to come and be available if there be a reason.

Treasurer Morley
Mark, concerning what you said, I have seen that the plan was once 100% funded and assumed investment rates of return were set up high at approximately 8, 8 ¼% rate of return knowing that we're operating on a principal of 70% equity, 30% bond and that would equate to a 10 1/2% return on equity and assuming a 10 1/2% rate of return on equity is unreasonable and what happened was the plan went from being approximately 100% funded down to about 78% funded, so my point with this is the City really didn't stay on top of that, it let it slip from 100 to about 78 through it's contributions.

Attorney Anastasi
I'm not in any position to dispute that but I think Tom from Segal might be able to answer it.

Tom Dawidowicz, Segal Company
We do an annual actuarial for the City and the comment about the 8% asset return which was very common across the country. Why the funded percentage went from 100% to roughly 80 somewhere in there had to do with the meltdown of the marketplace in 2008. Around the country there is a move to lower interest rates and probably a more common interest rate for pension plans is getting closer to 7 1/2 or maybe 7 1/4, so the history of using an 8% return and not achieving it really had nothing to do with the asset allocation unless you were strictly in cash you would have been hammered in 2008, 2009. If you had any equity exposure you probably got negative rate of return on your equities.

President Rosenberg
Isn't it also true that at one point your Company did an actuarial study and they misclassified the salaries of the fire fighters and there had to be a significant adjustment. There was a difference of over a million dollars in that particular year.

Tom Dawidowicz, Segal Company
That was a data error that the City had provided on to us. I don't recall what the number was.

Trustee Buck
Excuse me Tom, as of the last actuarial study, the current funding percentage on the pension plan.

Tom Dawidowicz
I haven't looked at the report; I think it was around 80% funded.

Trustee Buck
Knowing the way our agreement is scheduled with the contractual obligation for the City and that we've been comfortable at this relatively 8% level, as Jim properly stated out maybe there was some unrealistic percentages, now that we are changing the asset allocation to a much lower number of expected return, keeping that asset allocation knowing that there is a contractual obligation behind it.

Timothy Ryor
The goal is to leave the piece that's remaining after adjusting that interest rate to be exactly 100% funded. That was the purpose of the calculation. The point of debate is what is the right interest rate to use. If you agree that it's 4 1/4 then you need to have a plan that's 100% funded is 50.9 million.

Discussion of funding percentage.

Treasurer Morley
Question to Tom Dawidowicz, The Segal Company
A couple of reports ago, I think that Segal amended their actuarial assumptions to spread out the shortfall further over years.

Tom Dawidowicz
There were a couple of changes. There was a tweak in the asset evaluation method. The plan was already using what we call an asset smooth method. Unexpected gains and losses are deferred for future and spread over a longer period of time so you don't get hit when the market value returns. We recommended a tweak in that asset evaluation method. Nothing material, just a slight change in that. There may have been some changes in the amortization periods under GASBY. I remember working with the City in terms of the amortization period. GASBY, government accounting standard board allows pension plans to be funded over a thirty year period.

Treasurer Morley
What was the effect on the percentage of funding of making those changes.

Tom Dawidowicz
I don't recall. It's about two years ago.

Treasurer Morley
Did that cause the percentage of funding to go up or go down.

Tom Dawidowicz
I think the only change we made that would have reduced the funded percentage was lowering the interest rate that the City had been using. We recommended a lower rate as low as 8%. A reduction to 8% increased the liability pretty much what you see today. The lower the interest rate the higher the liability.

Treasurer Morley
Basically I'm seeing in the press that 8% is being considered to be unrealistic in today's market. Where do you stand on that Tom.

Tom Dawidowicz
We've been recommending lower interest rates for all of our clients and we've been moving in that direction.

Treasurer Morley
What was the assumed rate of return for your report for June 30, 2011.

Tom Dawidowicz
I think it was 8%.

Attorney Galiette
That's on an ongoing plan with ongoing contributions as opposed to a plan where it's basically going to be fixed.

President Rosenberg
Based on these figures I'm hearing the 4 ¼%, that was a net figure, so really what they're talking about is a 5% which is somewhere in the area what you just said, 5 or 6%. So, it would seem to me that you're pretty close.

Trustee Klein
Is it net or gross.

Tom Dawidowicz
I think it's net.

David Reiser
I will let you know what we talk about every day. The numbers that municipalities have been using over the years are completely unrealistic for a balance portfolio. I will tell you that historically with rates historically this low, the returns on a fixed income portion are terrible. They will either stay terrible or interest rates go up. Three years when we designed our new plan, I said that we were going to design a program based around the ERISA standards even though you didn't have to comply. We've lowered risk. Our firm feels that without COLAS, we feel the given life expectancy of our clients, we don't recommend anything greater than a 4% withdrawal rate or we're afraid that that client some day may run out of money. We can't give you a guarantee on anything in today's world. All we could try to do is give you in the current environment what we feel is hopefully achievable given what we've been doing with the portfolio.

Discussion regarding COLAS.

Attorney Galiette
Investment based on ERISA type of allocation and that is consistent with using the ERISA 4044 category allocation for determining the break out of the assets. It's an objective standard and I think previously you already determined that that would be a standard that you'd want to utilize at least refer to when calculating how much to turn over and how much to retain.

Trustee Klein
Would it be fair to say that the ERISA standard although we're not bound by it, but it would be prudent to follow it and the courts would probably apply it. Is ERISA standard a safe harbor.

Attorney Galiette
It's not a safe harbor, but using the ERISA standard is probably going to be the touch tone that a court would use to say whether you've acted prudently or not.

David Reiser
That's why we went that way three years ago.

City Attorney Anastasi
Am I not correct that the ERISA standard is intended to apply to a scenario where there is no expectation not only of regular funding on a go forward basis, but no contractual obligation for supplemental funding if a determination is made that is necessary. I raise that because there's some talk about being prudent and being careful and being cautious and being reasonable. I'm not the expert; I don't think the ERISA standard applies directly on that basis.

Attorney Galiette
The ERISA standard applies to the spinoff, a split up of two plans. It doesn't necessarily mean that one plan is terminating and the other one is continuing; it could be a split up of a plan to two ongoing plans which would have ongoing contributions.

Timothy Ryor
It's really a mechanism of achieving a certain funded ratio relative to the category of benefits. ERISA plans have contractual funding, so if you had two spinoff plans they would both have ongoing funding requirements. The point of the allocation is to say that at the point of time when you departed ways the plans were funded on a termination basis on the same basis they were prior to the split off.

Attorney Anastasi
Which is why and I don't know the gentleman's name, when he said if we're presently funded at around 80%, why is it that we're somehow obligated not to be funded on a conservative level at 100%. Because he said we were comfortable with that arrangement previously knowing you had the City having a contractual obligation and I realize the City is continuing to put money in, but it also had the active employees and it was putting it in.

Timothy Ryor
What I think that goes to is when you're talking about a funded ratio, you're generally talking about a single plan that has actives and inactives when you split it up, you want the inactives, you want them better funded than the actives. So if you split a plan up this is built into the ERISA allocation method you wouldn't expect the inactive portion to be the same percent funded as the active portion.

Attorney Galiette
Under ERISA it says that if there is a spinoff and a split off no one is suppose to get less of a benefit after the split off if they would have gotten before the split off if the plan had been terminated. So basically ERISA is looking to say we're splitting up the plan, we're calculating it as if the plan had terminated to spin off so that everyone is in the same position as if the plan had just closed down at that point.

Timothy Ryor
And you paid down the trust so what you do then is you pay everybody out according to the categories. You give the employees back their money first in proportion then you look who is in pay status and you pay them next and eventually you run out of money and so the people that are the lowest percent funded are going to be the actives.

Attorney Anastasi
I leave the debate on what the proper allocation is to the experts and I refer to Segal on our end, but I just want to make it very clear because I don't want anybody to think I'm arguing to the contrary, I want to be very clear that nothing the City has talked about doing was in any way, shape or form to not protect the retirees to the benefits that they were expecting prior to the split and that's why I keep coming back to the notion that the City recognizes its contractual obligation should an actuarial study show more funds are necessary. I understand the debate, but I want to make clear nobody thought the City was looking to walk away with less than a secure protection for the retirees.

Trustee Klein
What triggers the City's contractual obligation to kick in more money.

Attorney Anastasi
Section 13 of the pension agreement. Even though I believe Segal does an actual study every year, I believe the adjustment on the percentage contribution at least comes every year. That still points to the fact that the City recognizes its obligation. There's 100 ways to determine the appropriate amount of money and there are assumptions and there is also how conservative somebody wants to be, how risk adverse you want to be, but underlying it all is that ultimate obligation, that contractual obligation.

Trustee Rodriguez
In that contractual obligation, does it have to reach a certain percentage before the City kicks in.

City Attorney Anastasi
I think it has to be determined that it is not actuarially sound.

President Rosenberg
That would be actuarially determined not by our independent study, but by the City's actuary study.

Attorney Anastasi
It has always been done by the City's.

Tom Dawidowicz
We will continue to do the actual evaluation, compare the liabilities to the assets. If there is a shortfall, the assets are not 100% funded, the City will have to make a contribution.

President Rosenberg
One of the requirements under ERISA standards was for this Board to have an independent actuarial study. That's what we did. We could have used your Company's study, but we felt under advice of our counsel that that was not an independent study.

Tom Dawidowicz
First of all, I'm not disagreeing with Hooker & Holcomb's report and study. Two actuaries will have two sets of assumptions and they are both right and they are both wrong at the same time and you really don't know what the real answer is until the last person dies and look back and see what the cost was.

Attorney Anastasi
I want to stress that the City understands ultimately it is responsible to make sure the plan remains sound.

Discussion continued.

Trustee Klein motioned to accept the Report; Trustee Herlihy seconded and the Board passed it unanimously.

2. There being nothing further to come before the Board, Trustee Meszoros motioned to adjourn the meeting; Trustee Lee seconded and the Board passed it unanimously.

The meeting was adjourned at 7:45 p.m.