District of Columbia Retirement Board

Budget Oversight Hearing

Before the

Council of the District of Columbia
Committee of the Whole

April 17, 2015

OPENING REMARKS

Good afternoon, Chairman Mendelson and members of the Council of the District of Columbia Committee of the Whole. I am Eric Stanchfield, Executive Director of the District of Columbia Retirement Board (DCRB). I would like to thank Trustee Lyle Blanchard for his introduction and for taking the time to represent DCRB's Board of Trustees before this Committee. I will testify on our FY 2016 Budget.

Joining me today to respond to the Committee's questions are Sheila Morgan-Johnson, Chief Investment and Chief Operations Officer; Johnetta Bond, Chief Benefits Officer; Anthony Shelborne, Controller; as well as Ed Koebel, of Cavanaugh Macdonald, our independent actuary. Other senior staff in attendance include Erie Sampson, General Counsel; Peter Dewar, Chief Technology Officer; and Joan Passerino, Director of Stakeholder Communication and Outreach.

DCRB was created by Congress in 1979 under the District of Columbia Retirement Reform Act as an independent agency of the District of Columbia government. The Agency has exclusive authority and discretion to manage the assets of the District of Columbia Teachers' Retirement Fund and the District of Columbia Police Officers and Fire Fighters' Retirement Fund (collectively referred to as the "Fund") and to provide our members with a range of retirement administration services. Our mission is to provide these services to our members from their date of initial participation in the District of Columbia Teachers' Retirement Plan and the District of Columbia Police Officers and Firefighters' Retirement Plan (collectively referred to as the "Plans") throughout their lifetime and their survivors' lifetime, and to safeguard the integrity of the Fund.

DCRB invests and manages the Fund, which is held in trust for the exclusive benefit of all Plan members and their eligible survivors and beneficiaries. The assets of the Fund, which are commingled for investment purposes, can only be used to pay benefits to Plan members and associated administrative expenses.

DCRB's Board of Trustees (the "Board") has 12 members, six (6) who are elected by members the Plans, three (3) who are appointed by the Mayor, and three (3) who are appointed by this Council. In addition, the Deputy CFO/Treasurer serves on the Board as an ex-officio (non-voting) member (representing the

District's CFO). Board members are fiduciaries, who are required to discharge their responsibilities solely in the interest of Plan members and beneficiaries.

The District government, as the employer, is the Plan Sponsor and is responsible for the design of the Plans and for paying the required employer contributions to the Fund. DCRB, as Plan Administrator, is responsible for investing the assets of the Fund and for providing a range of pension administration services to our members. DCRB also serves as the third-party administrator for benefits under the frozen federal plans for District police officers, firefighters, and teachers for which the U.S. Department of the Treasury (Treasury) is responsible.

As of September 30, 2014, the Plans had 23,982 members. Of this number, 13,932 were retirees and survivors who receive monthly pension payments, and 10,050 were active employees. As of September 30, 2014, the Fund was valued at $6.3 billion, an increase of approximately $540 million in net asset value over the previous 12 months. During Fiscal Year 2014, members received approximately $120 million in benefit payments from our trust.

I am pleased to report that as of October 1, 2014, the Plan's aggregate funded ratio was 101.4 percent. For the individual Funds, the ratios were: Teachers' at 88.6 percent, and Police and Firefighters' at 107.3 percent.

DCRB'S STRATEGIC GOALS

I would like to highlight our current and upcoming initiatives aimed at achieving our strategic goals during FY 2015, and discuss how our budget for FY 2016 will help us further those goals.

1. Expand and improve member benefits administration capabilities while assuring benefits are paid to our members timely and accurately.

Three years ago, DCRB launched a multi-year, Retirement Modernization Program focused on the areas of benefits administration and information technology. The Program includes three main projects: Business Process Reengineering ("BPR"), Data Reclamation, and a Pension Information Management System ("PIMS").

Under BPR, the Benefits Department reconfigured existing workflows; restructured the Department; redefined and developed new roles; performed staff skills assessments; and delivered targeted training. Data Reclamation involved establishing a database of service, salary, and contribution history that will reduce the processing time required to pay initial pension payments.

The PIMS will enable DCRB to provide a full range of retirement services for members—including benefits statements, benefit estimates, member self-service, and the integration of pension data into systems designed to produce pension payments.

During FY 2015 and FY 2016, DCRB plans to implement an Enterprise Data Quality tool and a Master Data Management (MDM) system that will allow DCRB to collect Plan member information from multiple systems into a single data source. This MDM system will gather data from the District's PeopleSoft active member repository and from Treasury's STAR annuitant system, and aggregate the information in a database that will become a single source for maintaining the Plan. All of these efforts are intended to provide accurate benefit payments, reduce reliance on paper documents, and minimize the turnaround time to deliver initial pension payments. This will also provide members with access to important pension-related information prior to retirement that will enhance their retirement planning decisions.

2. Prudently invest Fund assets to provide long-term sustainable risk adjusted returns.

DCRB's ongoing objective is to prudently manage Fund assets with the goal of earning a return that meets or exceeds the actuarial investment return target of 6.5% over the long-term. We measure Fund performance against several benchmarks and compare our investment costs to industry peers of similar asset size and allocation. In addition, we frequently evaluate potential rebalancing opportunities within the Fund to ensure that the various asset classes are within our strategic target ranges. Further, we are conducting searches for investment consultants and a custodial bank, each targeted for completion in FY 2015. During FY 2016, DCRB and the investment consultant will review the Fund's asset allocation and manager structure.

3. **<u>Refine DCRB's organizational structure to meet agency responsibilities and needs.</u>**

In FY 2014, an Audit Committee charter was formally established. One key responsibility of this Committee is to provide independent review and oversight of DCRB's financial reporting processes and internal controls. In addition, DCRB will train and prepare its staff to use new applications and systems that will improve our operations. One example is a system being developed to certify the service, salary and contributions of plan members on an ongoing basis, rather than the current process of certifying this data when they retire. This change is intended to reduce the timeframe for initial pension payments.

4. **<u>Foster member and stakeholder trust through enhanced communications and collaborative outreach</u>.**

DCRB plans to enhance staff efficiency by developing intranet capabilities (an "employee portal") that will encourage and facilitate collaboration through improved staff communication and information sharing.

The employee portal will enable DCRB to become a more technology secure information-sharing organization. In this future state, authorized staff will be able to access information remotely in the event of a disaster.

In addition, DCRB will enhance its outreach and collaboration with stakeholder agencies. For example, in March 2015, DCRB joined with DCPS to offer teachers a retirement workshop, which was hosted at DCRB. We are talking with DCPS about offering more frequent workshops at several locations and times.

5. **<u>Safeguard the integrity of the Fund</u>.**

We will increase our protective capabilities to counter the threat of cyber-attacks. The Agency continues to develop its security framework using current industry practices and technology, as well as knowledgeable resources.

Our governance of business processes in the area of information technology will be enhanced by seeking the International Organization for Standardization (ISO) certification. This will allow us to standardize service delivery and project management.

Finally, in FY 2015, we are again undertaking an actuarial audit, which will be completed by an independent actuarial firm. This review provides an additional set of “eyes” and technical expertise to review our independent actuary’s assumptions and calculations.

Now I will discuss our proposed FY 2016 operating budget. DCRB manages the Fund, receives contributions, and calculates and pays benefits for qualifying members upon retirement, termination, disability, or death.

In addition, as mentioned earlier, DCRB serves as the third-party benefits administrator for the frozen federal plans supported by Treasury, receiving a payment from Treasury for these administrative services. That payment is anticipated to be $3.6 million for FY 2015 and $3.8 million for FY 2016.

Under the line item, Agency Management, DCRB’s FY 2016 budget reflects the following seven budgetary activities under the Executive Director’s oversight: Investments, Benefits, Operations (which includes Finance), Information Technology, Legal, Projects and the Executive Office. An eighth budgetary activity is under the Board of Trustees.

For several years, DCRB’s budget was $30.3 million. With the retirement modernization projects now accelerating, we anticipate expending a greater portion of our approved budget.

DCRB’s FY 2016 budget is $32.3 million. For several years, we spent substantially less than our approved budget. Although we are expending a larger percentage of the approved budget, our budget as a percentage of assets continues to decline.

The budget includes 62.6 authorized full-time employees (FTEs), an increase of 5.0 FTEs from the FY 2015 level. As in the past, we will continue to fill positions as needed for the prudent management of investments, benefits administration, increased communications, and effective internal control of the accounting, legal and procurement functions.

In the proposed budget for FY 2016, there are two broad areas of change:

- The Personnel Services budget is $8.1 million, reflecting an increase of $0.9 million over the FY 2015 amount. The increase includes an overall addition of 5.0 FTEs for: benefits administration, agency operations, investments, and benefits accounting. The positions will allow us to improve member services in the Benefits Department, assist the Investment Department with monitoring and compliance issues, and help the Information Technology Department with the implementation and ongoing maintenance of several systems that are designed to support the agency's mission.

- The Non-Personnel Services budget is $24.2 million, reflecting an increase of $1.1 million from the FY 2015 amount. The increase primarily supports estimated investment manager fees that have grown along with the Fund's assets.

On a line-item basis, DCRB's FY 2016 Budget varies from FY 2015 across the following Comptroller Source Groups (CSG):

<u>CSG 11 Regular Pay- Continuing Full-Time</u>: An increase of $649,000 for the cost-to-continue adjustments, as well as the additional staff mentioned above. As we move ahead with the implementation of our strategic plan of enhanced services and technology improvements, DCRB will need to increase staffing levels.

<u>CSG 14 Fringe Benefits</u>: An increase of $184,000 for projected fringe benefit costs related to CSG 11 Regular Pay.

<u>CSG 20 Supplies and Materials</u>: A net decrease of $111,000 based on estimates derived from recent actual expenditures.

<u>CSG 31 Rent</u>: A decrease of $23,000 to reflect the lease expenses we are incurring.

<u>CSG 40 Other Services and Charges</u>, and <u>CSG 41 Contractual Services</u>: An increase of $1.8 million, largely due to an increase in investment related costs, including custodial fees and consulting expenses. The investment

management expenses, as indicated previously, are based on assets under management and fluctuate from year to year.

CSG 70 Equipment and Machinery: A decrease of $578,000 reflects the fact that we purchased more equipment in FY 2015 to install in our newly renovated space. It also reflects DCRB's technology shift to a virtual environment, which does not require the physical equipment and machinery of past years. This shift decreases our equipment needs in the short-term.

My next comments relate to the District's certified FY 2016 contribution to the Fund. The District annually contributes an amount to the Fund that is equal to the "Normal Contribution Rate" determined by DCRB's independent enrolled actuary. This is the amount required to keep the Plans funded on an actuarially sound basis, taking into account: (1) anticipated future employee contributions, (2) assets in the Funds, and (3) projected future investment earnings of the Funds. The Board certifies this amount to the Mayor and the Council for inclusion in the District's approved budget for the ensuing fiscal year. This process is a sound mechanism for funding benefit promises when they are made and assures that pension contributions remain relatively stable as a percentage of covered payroll over time.

The District's certified Normal Contribution for FY 2016 is $180.6 million. As prudent fiduciaries, these contributions plus investment earnings will create reserves for the expected "crossover point" where payouts will exceed contributions. This is the norm for a "mature" pension plan. As a general rule, employer contributions for all groups will rise as salaries increase, assuming other actuarial assumptions are met. The key drivers that can change the annual contribution include the recognition of investment gains or losses, wage and general inflation, differences in assumed versus actual retirement and mortality rates, as well as changes due to labor contract negotiations and legislation. As I mentioned, our independent actuary is here to answer any questions you may have on DCRB's contribution rates and funding status.

In summary, I am pleased to report that the Fund is in excellent shape. Our Board has maintained conservative investment assumptions, the Plan is in sound financial condition, and we pay members timely. We have a skilled Board and an experienced team managing our strategic initiatives. And, most importantly, we continue to make strides toward creating a comprehensive retirement system to serve the needs of our members.

In closing, I'd like to thank the Committee for your support in helping us to carry out this mission. As we proceed, we may seek your assistance in helping us accomplish our goals. We look forward to working with you and your staff.

This concludes DCRB's Budget Oversight Hearing Testimony. We look forward to answering your questions. Thank you.