BUDGET OVERSIGHT HEARING ON THE DISTRICT OF COLUMBIA RETIREMENT BOARD PROPOSED BUDGET FOR FISCAL YEAR 2019

Testimony of

Sheila Morgan-Johnson, Executive Director
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Before

The Honorable Phil Mendelson, Chairman
Committee of the Whole
Council of the District of Columbia

John A. Wilson Building, Room 120
1350 Pennsylvania Avenue, NW
Washington, DC 20004

March 27, 2018

OPENING REMARKS

Good afternoon, Chairman Mendelson and members of the Council of the District of Columbia Committee of the Whole. I am Sheila Morgan-Johnson, Executive Director of the District of Columbia Retirement Board (Board or DCRB). I will testify on DCRB's Proposed FY 2019 Budget.

Joining me today to respond to the Committee's questions are Anthony Shelborne, Chief Financial Officer; Johnetta Bond, Chief Benefits Officer; and Ed Koebel, our independent actuary of Cavanaugh Macdonald,

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 Board 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"). Our mission also includes providing a range of retirement administration services for members of the District of Columbia Teachers' Retirement Plan (the Teachers' Plan) and the District of Columbia Police Officers and Firefighters' Retirement Plan (the Police Officers and Firefighters' Plan) (collectively referred to as the "Plans") throughout their lives and the lives of their survivors.

The Board 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. 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 benefits administrator for District police officers, firefighters and teachers, who are covered under retirement plans that were frozen prior to July 1, 1997 and funded by the U.S. Department of the Treasury (Treasury).

As of October 1, 2017, the total membership of the District Replacement Plans and the frozen (federally-funded) plans was 26,433 members. Of this number, 14,252 were retirees and survivors who receive monthly pension payments, 10,511 were active employees, and there were 1,670 former members who are vested with a deferred benefit. During FY 2017, approximately $175 million was paid out in benefit payments from the Fund.

As of September 30, 2017, the Fund was valued at $7.8 billion. By the end of February 2018, the assets of the Fund had grown to $8.2 billion.

I am pleased to report that as of October 1, 2017, the Plans' aggregate funded ratio was 105.2 percent. For the individual Plans, the ratios were: 92.5 percent for the Teachers' Plan, and 110.8 percent for the Police Officers and Firefighters' Plan.

PROPOSED OPERATING BUDGET

As noted above, DCRB's mission includes two overarching goals: 1) to prudently invest the assets of the Fund for the exclusive benefit of Plan members, and 2) to provide Plan members with a range of retirement services. I would like to highlight our current and upcoming initiatives aimed at achieving our strategic goals during FY 2017 and FY 2018 and discuss how our budget for FY 2019 will help us further those goals.

The Board of Trustees has reviewed and approved the Agency's proposed operating budget for FY 2019 of $43.6 million, a 4.6 percent increase ($1.9 million) over FY 2018, and a staff of 75 FTEs, which is the same as last fiscal year. Although various object classes may be somewhat different from last year, the overall increase is primarily due to maintaining our current staffing levels and investment-related expenses. The differences between the FY 2018 and the FY 2019 budgets are explained below.

Executive – Decrease of 14.5 percent ($291 thousand)

To assure that our salaries and pay structure are comparable to other retirement systems and competitive with the regional market, DCRB began a Classification and Compensation Study late last year. We also planned to begin an update of our Strategic Plan, which will include a review of our organizational structure to ensure that it will continue to support our goals and projects going forward. The decrease of $291 thousand reflects a change in priorities for the Agency such that these projects were not completed when originally expected. In addition, we have revamped our Summary Plan Descriptions (SPDs) and will distribute them to Plan members next month. With respect to these pension booklets and our quarterly newsletters, we are transitioning from paper documents to electronic versions this year, which will serve to reduce costs both this year and in the future.

Investments - Increase of 17.2 percent ($2.4 million)

Since investment fees reflect the level of the assets in the Fund, we estimate the growth or reduction of the assets, and project changes in the investment fees accordingly. Applying this methodology, the Investment Department budget for FY 2019 shows an increase of $2.4 million over FY 2018. Unless the market direction changes, we expect that investment fees will continue to grow.

Benefits – Increase of 8.1% ($286 thousand)

This budget increase of $286 thousand reflects the cost of maintaining salaries and fringe benefits for current FTEs.   It also reflects potential salary increases that may occur as a result of the Class and Compensation Study as mentioned earlier.   The Benefits Department will be able to maintain its current staffing level and provide enhanced services, which this past year included issuing estimated Benefits Statements to active firefighters. This year and hereafter, estimated Benefit Statements will be sent to all active police officers, firefighters and teachers. There were no decreases in non-personal services. DCRB will continue to work collaboratively with our stakeholders to provide high quality service to Plan members.

Operations – Decrease of 5.0% ($216 thousand)

The decrease of $216 thousand is the result of nonrecurring contractual and consulting expenses in FY 2019.

Information Technology (IT) – Increase of 1.1 percent ($93 thousand)

This budget increase of $93 thousand reflects the cost of maintaining salaries and fringe benefits for current FTEs. As with the Benefits Department, IT will be able to maintain its current staffing level until the Pension Information Management System (PIMS) project begins. During FY 2017, we achieved compliance with the Federal Information Security Management Act (FISMA) for information systems operations. During FY 2018 and beyond, the IT Department has ongoing projects focused on updating our disaster recovery and continuity-of-operations plans. In addition, IT is currently working with the Benefits Department on developing a self-service portal for our website that will allow annuitants to login and review pension-related information. Phase 2 of that project, which is expected to begin in FY 2019, will allow annuitants to make changes online including changes to their addresses, bank information, and tax withholding.

Projects – Decrease of 3.8 percent ($291 thousand)

The FY 2019 budget was developed assuming that certain phases of the PIMS project would be delayed. Since that project had originally been scheduled to begin during FY 2018, there is a decrease of $291 thousand in start-up costs that will shift to FY 2020. Consequently, we reduced contractual and consulting expenses for FY 2019.

Personal Services (Increase of $435 thousand)

The proposed budget for Personal Services is $10.9 million. As already noted in the departmental budget comments, there will be no increase in FTEs during FY 2019. Although there is no increase in staff, we anticipate an increase in costs of $435 thousand, due to salary increases and fringe benefit costs.

Non-Personal Services (Increase of $1.5 million)

The Non-Personal Services proposed budget for FY 2019 is $32.6 million, of which $14.7 million is projected for investment-related fees and expenses. As also noted in the departmental budget descriptions, the Non-Personal Services proposed budget increase of 4.8 percent ($1.5 million), from the FY 2018 amount, is primarily the result of a conservative estimate of the rate of growth of Fund assets. Investment manager fees fluctuate in tandem with the assets under management. DCRB consistently monitors and negotiates fees to ensure that the fees we pay are reasonable and reflective of the services provided by investment service providers.

It is important to note that Treasury reimburses DCRB for the third-party benefits administrator services for the frozen federally-funded plans. The amount received from Treasury is anticipated to be $3.3 million for FY 2018 and $3.9

million for FY 2019. I wish to point out that DCRB also makes a payment to Treasury each fiscal year, as part of the cost-sharing agreement for payroll services, postage expenses related to the benefits payments of our members, and maintenance and system upgrade expenses related to the System to Administer Retirement, also known as STAR. The payments to Treasury average about $1.3 million annually, and the amount budgeted for FY 2019 for these services totals $1.6 million. These dollar amounts are reflected in the FY 2019 $43.6 million budget. Finally, as in prior years, any unspent budget amounts remain in the Fund.

FY 2019 REQUIRED DISTRICT PAYMENT TO THE FUND

The District's certified FY 2019 contribution to the Fund is $144.6 million. The Teachers' Retirement Fund's proposed contribution of $53.3 million represents a $5.7 million decrease from FY 2018, while the Police Officers' and Fire Fighters' Retirement Fund's proposed contribution of $91.3 million declined by $14.3 million from FY 2018. The $144.6 million is the employer contribution amount certified by the Board's independent actuary as the actuarially determined employer contribution, or ADEC, for FY 2019. The decreases are the result of lower actual cost-of-living and salary increases than those projected to occur in the economic assumptions for the Plans as well as our great investment returns. The Board certified this amount to the Mayor and the Council in January 2018 for inclusion in the District's approved budget.

These contributions plus investment earnings will create reserves for the expected "crossover point" (in approximately 2019 through 2023) where payouts in benefits is expected to exceed contributions for each of the Plans. This is an expected occurrence as the Plans mature. 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 and funded status.

CONCLUSION

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, we continue to make strides toward creating a comprehensive retirement system to serve the needs of Plan 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.