



**PERFORMANCE OVERSIGHT HEARING ON
THE DISTRICT OF COLUMBIA RETIREMENT BOARD
FOR FISCAL YEAR 2017**

Testimony of

Sheila Morgan-Johnson, Executive Director
District of Columbia Retirement Board

Before the

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

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OPENING REMARKS

Good morning Chairman Mendelson and members of the Committee of the Whole. I am Sheila Morgan-Johnson, Executive Director and, for the moment, the Chief Investment Officer for the District of Columbia Retirement Board (DCRB or the Board). I am pleased to testify, for the first time as DCRB's Executive Director, on DCRB's FY 2017 performance. With me today to also respond to the Committee's questions are Ed Koebel of Cavanaugh Macdonald Consulting, our independent actuary, and Johnetta Bond, Chief Benefits Officer, as well as other members of DCRB's Executive Management Team. Before discussing the mission and priorities of DCRB, I would like to acknowledge the guidance and support provided by our Board of Trustees and the assistance of this Committee and your staff over the past year.

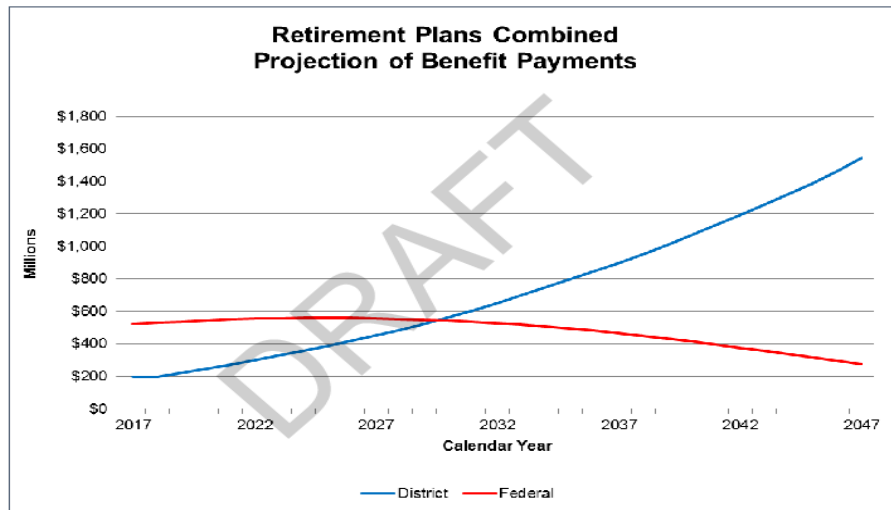
MISSION

DCRB was created by Congress in 1979 as an independent agency of the District of Columbia Government. The Board is a fiduciary that has the 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"). These assets are held in trust for the sole benefit of members of the District of Columbia Police Officers and Firefighters' Retirement Plan and the District of Columbia Teachers' Retirement Plan (referred to as the "Plans"), as well as their eligible survivors and beneficiaries.

The District is responsible for members covered under the District Replacement Plans, which were adopted on July 1, 1997. Fund assets, which are pooled for investment purposes, may only be used to pay benefits and expenses necessary to administer the retirement program. DCRB also serves as the third-party administrator for benefits earned through June 30, 1997, under the frozen federal plans, which are the responsibility of the U.S. Department of the Treasury.

For the District Replacement Plans, 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 into the Fund. In addition to employer contributions, trust income includes employee contributions, which are a fixed percentage of their pay, and earnings on investments.

As of September 30, 2017, the total membership of the District Replacement Plans and the federal frozen plans was 26,433. It should be noted that approximately 73 percent (19,295) are now members of the District Replacement Plans and/or jointly funded by the District and federal governments. Although the current majority of benefit payments are paid by the U.S. Treasury for accrued federal benefits, the District is becoming more responsible for an increasing portion of the total benefits. The following table shows that District benefit payments are expected to exceed federal benefit payments around 2030.



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Next month, the Board’s independent actuary will present the results of a Thirty-Year Projection Study. This study will develop a picture of each Plan’s funding progress over time and estimate the future assets, liabilities, contributions and benefit payments for each of the Plans. The study also will serve as a planning tool to guide investment decisions and help ensure that the applicable pension liabilities and funding mechanisms are managed in a manner that promotes sustainability.

As illustrated above, the percentage of pension benefits paid will become more a District than a federal liability. Consequently, the Board intends to place a greater emphasis on modernizing retirement administration and preserving Fund assets to maintain the Plans’ strong actuarial funded ratios.

The Board’s independent actuary reports that the aggregate actuarial funded ratio for the District Plans was 105.2 percent as of October 1, 2017. The individual Plan ratios were: 92.5 percent for the Teachers’ Plan and 110.8 percent for the Police Officers (111.2 percent) and Firefighters’ (109.9 percent) Plan, as of the same date.

As of September 30, 2017, the market value of the Fund was \$7.8 billion, an increase of approximately \$975 million in total asset value over the previous 12 months. As of January 31, 2018, the assets in the Fund increased to \$8.4 billion.

DCRB’s work continues to be guided by its two-fold mission: (1) to prudently invest and manage the assets of the Fund and (2) to administer retirement benefits. Agency operations are managed in accordance with our fiduciary responsibilities and relevant legal authorities. The projects and initiatives discussed in my testimony support this mission.

Invest and Manage Fund Assets

One of DCRB’s major ongoing responsibility is to prudently manage the Fund assets, with the goal of earning a return that meets or exceeds our actuarial investment return assumption. The Board has established an actuarial return target of 6.5 percent to sustain the Fund’s viability over the long-term

investment horizon. I am pleased to report that, since its inception in October 1982, the Fund has generated an annualized gross return of 8.9 percent, surpassing the actuarial return target by 2.4 percent per year. For FY 2017, the Fund earned a gross return of 13.1 percent, outperforming the actuarial target and benchmark. In building a solid foundation for achieving long-term, sustainable risk-adjusted net returns, we routinely review investment manager performance against benchmark returns, rebalance the portfolio to maintain compliance with asset allocation targets and ranges, and monitor and evaluate fees.

In addition to systematically reviewing the investment performance and operational processes of investment service providers, DCRB completed the following investment activities:

- Updated asset allocation targets to reflect the results of the 2016 asset allocation study to ensure the continued alignment of the Board's asset allocation policy with the long-term liability structure. An asset allocation review will be conducted in FY 2018 to position the Fund for unforeseen market volatility.
- Offered continuing education to Trustees and Staff on investment and regulatory matters, including fiduciary responsibilities, risk management and mitigation, and investment compliance.
- Reviewed the funding goals and benchmarks of the Board's Funding Policy that were adopted in 2012 and made a revision to include a change in the asset smoothing period from seven years to five years, and a change to the amortization methodology.

Further, during FY 2017, Investment staff conducted extensive research on opportunities for additional exposure to emerging and diverse managers. Staff considered best practices for constructing and deploying an emerging and diverse managers program, the operational risks associated with investing with private markets emerging and diverse managers, and the positions taken by other similarly situated retirement systems on the use of such managers. In January 2018, after discussions with staff and leading industry experts, the Board approved an initiative focused on building and managing a stable of private markets emerging and diverse managers.

Benefits Administration

Another of DCRB's major responsibilities is to administer retirement benefits. Among our primary tasks is to ensure the timely and accurate payment of benefits to Plan members, their survivors and beneficiaries. We also provide members with services, provide information about the plans, answer their questions, and keep them aware of changes and issues related to their benefits.

Retirement Modernization

Through the use of technology, DCRB is automating manual processes and digitizing member records to reduce the reliance on paper documents.

Annual Benefits Statements

During FY 2017, DCRB successfully issued annual benefits statements to all active District firefighters. During FY 2018, DCRB will deliver annual benefits statements to all active members of the Plans.

Self-Service Application

Over the past year, DCRB has worked to develop a self-service application to allow retired annuitants to access their benefit- and tax-related information. This initiative will align DCRB more closely with its peers in terms of ease of access to information for annuitants. This is anticipated to reduce the number of calls and visits to DCRB for routine questions and updates.

Initially, the self-service application will allow annuitants to view and print personal information such as earnings statements, current contact information, tax withholding elections, and beneficiary designations, as well as DCRB standard forms. DCRB also will use the application as an additional mode of communication with annuitants, to timely provide updates on issues pertinent to our Plan members. The self-service application is anticipated to be expanded, at a later date, to allow members to also make updates to their personal information within the application itself.

Other Retirement Modernization Efforts

During FY 2017, DCRB achieved compliance with the Federal Information Security Management Act (FISMA) for information systems operations. This effort was part of the comprehensive information security framework DCRB has implemented to reduce the risk of data loss and maintain the confidentiality of personally identifiable information from cybersecurity threats. Further, as business continuity is critical to our agency, DCRB has ongoing projects focused on updating our disaster recovery and continuity-of-operations plans.

Finally, DCRB will release a solicitation for a system to electronically manage District pension-related information in one place. This system will be configured to allow DCRB to provide a full range of retirement services for Plan members.

Legislative and Compliance Initiatives

2017 Summary Plan Descriptions

DCRB undertook a comprehensive review and update of the Summary Plan Descriptions (SPDs) for each of the Plans. The new SPD will clarify Plan provisions, benefits administration policies and processes, and summarize the provisions of the Plans in a format that is easier for Plan members to read and understand. The SPDs will be distributed during FY 2018 to all Plan members.

Technical Amendments to the District Replacement Plans

On September 25, 2017, Bill 22-468, the Teachers', Police, and Firefighters Retirement Benefits Technical Amendment Act of 2017 was introduced. The bill:

1. clarifies that the same provisions of the District Replacement Plans that are affected by marriage will also apply to domestic partnerships;
2. addresses how 401(a) plan monies may be transferred by a member into the District of Columbia Police Officers and Fire Fighters' Retirement Fund towards the purchase of his/her prior service; and

3. clarifies the application of the Internal Revenue Code § 401(a)(17) compensation limit to members first covered under the Plan on or after October 1, 2002. The public hearing on this bill is scheduled to be conducted this afternoon. DCRB staff will testify at the hearing and answer questions from the Council and the public.

Updated Board Rules

DCRB recently issued a Notice of Proposed Rulemaking to update the Board Rules which currently comprise Chapter 15 of Title 7 of the District of Columbia Municipal Regulations and set forth the Board's organizational structure and operational components. The Board proposed to extend Chapter 15 to include the provisions governing the election of Board Trustees who represent active and retired teachers, police officers, and firefighters. The Board approved the proposed Board Rules on September 26, 2017. The Notice of Proposed Rulemaking was published in the District of Columbia Register on February 9, 2018, and will remain available for public comment for a minimum of 30 days.

Strategic Planning & Initiatives

As this is my first year as Executive Director of DCRB, I will set the course for DCRB's continued advancement under my leadership. This will require a re-evaluation of the agency's current goals and objectives to ensure that they continue to align with DCRB's mission. This year, the Board and DCRB's leadership team will engage in a comprehensive strategic planning process to:

1. identify and prioritize initiatives;
2. assess the agency's ability to perform in a primarily electronic or digital benefits administration environment; and
3. adjust and focus the agency's resources around common goals with well-defined results.

A comprehensive strategic plan will be especially important with the approaching acquisition of a pension information management system, the growth of the Fund, and the increased membership in the District Replacement Plans.

CONCLUSION

In summary, I am pleased to report that the Fund is in sound financial condition and that we pay Plan members accurately and timely. Further, the Board's trustees are engaged and committed to our mission, and we have a knowledgeable and experienced senior team managing the Agency's strategic initiatives. Together, we continue to move forward in creating a comprehensive retirement administration system to serve the needs of Plan participants over the long-term.

In closing, I'd like to thank you for your leadership and support. I am happy to answer any questions you may have.