MINUTES

Public Retirement Systems Committee

LEGISLATIVE SERVICES AGENCY

Serving the Iowa Legislature

Wednesday, December 9, 2015

MEMBERS PRESENT

Senator Thomas G. Courtney, Co-chairperson
Senator Jeff Danielson
Senator Matt McCoy
Senator Charles Schneider

Representative Dawn E. Pettengill, Co-chairperson
Representative Gary Carlson
Representative Kevin Koester
Representative Vicki S. Lensing
Representative Mary Mascher

Organizational staffing provided by: Ed Cook, Senior Legal Counsel, 515-281-3994; Minutes prepared by: Andrew Ward, Legal Counsel, 515-725-2251

CONTENTS

I. Procedural Business

Call to Order and Adjournment. The meeting of the Public Retirement Systems Committee was called to order by temporary Co-chairperson Representative Pettengill at 10:10 a.m., Wednesday, December 9, 2015, in Room 103, Supreme Court Chamber, State Capitol, Des Moines. The meeting was adjourned at 3:30 p.m.

Election of Permanent Co-chairpersons. Members of the committee unanimously elected temporary Co-chairperson Pettengill and Co-chairperson Courtney as permanent Co-chairpersons.

Adoption of Rules. Members of the committee unanimously adopted procedural rules for the committee.

Opening Remarks. Co-chairperson Pettengill described the role of the Legislature in overseeing the various state pension systems and the committee's role in providing regular oversight of system governance and performance. Co-chairperson Courtney expressed his appreciation for having the privilege to serve on the committee and stressed the importance of the committee's work.

II. DAS — Retirement Investors' Club

Ms. Janet Phipps, Director, Department of Administrative Services (DAS), described the Retirement Investors' Club (RIC) as a supplemental retirement savings program providing Internal Revenue Code sections 457, 401(a), and 403(b) plan administration. Ms. Phipps stated that RIC plans are intended to supplement fixed retirement programs, providing a benefit for employees and encouraging them to think about their retirement. Ms. Phipps described sections 457 and 401(a) plans as doors for state employees, and other public sector employees, to enter into the RIC, while section 403(b) plans are doors for education employees to have access to RIC. She described RIC's authorizing legislation, program requirements, and associated employer contributions.

Ms. Phipps discussed the separate Request for Proposals (RFP) and Invitation to Qualify (ITQ) processes for selecting plan providers, noting that RIC "core providers" went through the RFP process, and noting that core providers needed to satisfy certain program requirements, including low maximum fees and no surrender penalties. She then described the expansion of section 403(b) offerings to include additional providers available after the ITQ process, and stating that individual school districts can decide whether or not to offer plan options from the additional providers.

Ms. Phipps described the process of entering into agreements with the core providers and the interest among employees for the broader range of products offered by the additional plan providers. Ms. Phipps stated that she was unsure of the impetus behind offering additional providers to section 403(b) education employees, while not making the additional providers available to section 457 and section 401(a) employees. In response to a question from Co-chairperson Pettengill, Ms. Phipps confirmed that Voya, a core provider, serves as the common remitter for the RIC program at no cost, distributing contributions to those providers selected by plan participants. She stated that, to her knowledge, Voya's common remitter role was not contingent to Voya also being a core provider. Ms. Phipps stated that DAS communicates with most eligible employees through direct e-mails, but, for legislative employees, instead communicates with human resources officials.

Responding to Co-chairperson Pettengill, Ms. Phipps confirmed that more than 300 school districts pay DAS $400 each per year to manage the RIC section 403(b) program, and noted that this provides efficiency of scale benefits to school districts that seek to offer supplemental retirement benefits to their employees. She stated that DAS is an enterprise agency and does not rely heavily on General Fund appropriations. Co-chairperson Pettengill opined that it was peculiar that taxpayers paid for plan administration rather than plan participants and that the warning notices on enrollment forms could be barriers dissuading employees against plans that might serve them best. Ms. Phipps stated that DAS will reevaluate those notices, but stated that the notices serve to encourage the participants to ask informative questions.

In response to a question from Representative Carlson, Ms. Phipps noted that DAS can better communicate with school districts on DAS oversight and the transferability of DAS services, related to both core and additional plan services.

Ms. Phipps stated that school districts choose whether or not to opt into the RIC program, and that participating districts then select whether to offer only core provider options or to offer core and ITQ-selected providers. She stated that a district that chooses to offer plans offered by the ITQ-selected providers will not incur any additional costs. She noted that school districts are still making their decisions on plan offerings, and that DAS does not yet have information on school districts' choices. She further clarified that districts may not select from among the additional providers, but must choose whether to offer all or none of the ITQ-selected additional providers.

Senator McCoy opined that the plan document should more clearly delineate school district choices between the core and ITQ-selected providers and detail DAS plan administration for both types of plan offerings. Ms. Phipps noted that the enrollment form will provide school districts with information on their particular plans.

Representative Koester stated that the additional ITQ plan offerings provided good free market options to employees, while noting the significant increase in administrative fees charged by the ITQ-selected providers. He stated that school districts should be aware of and educate employees of the differences between core and ITQ-selected providers. In response to a question from Representative Koester, Ms. Phipps noted uncertainty as to whether school business officials face any additional legal or financial liabilities by expanding plan offerings to include the optional plan providers. She stated that she would investigate this issue.

Mr. Brad Hudson, Iowa State Education Association, provided information on the history of school district participation in the RIC program, noting that school districts have offered core provider plans since 2008 and that some districts may offer the ITQ-selected plans for the first time starting in 2016. Mr. Hudson noted that plan documents need to meet Internal Revenue Service (IRS) guidance, and stated that districts, as plan providers, bear some responsibility in vetting providers. Ms. Phipps stated that the RIC plan document is currently being amended to include the ITQ-selected plan offerings, and noted that no legislative changes are necessary to expand the RIC program to include ITQ-selected providers. She also noted the benefits of scale in providing statewide administration of these plans for districts, instead of 300+ benefit administration systems for each participating school district.

Representative Carlson and Ms. Phipps discussed the school district enrollment and transferability process with relation to DAS monitoring of participating employees contribution caps under IRS regulations. Ms. Phipps noted that DAS bears the same administrative burdens related to both core and ITQ-selected providers.

Co-chairperson Pettengill noted DAS oversight in selection of both core and ITQ-selected providers and opined that there must have been some degree of scrutiny of optional providers since only five ITQ-selected providers were approved pursuant to the ITQ process. Ms. Phipps then noted RIC participation rates as of June 30, 2015, and noted that she will provide information on the number of ITQ-generated applicants to the committee. Senator McCoy inquired whether, and Ms. Phipps confirmed that, the amended plan document for the RIC program would include information on the four core providers and the five ITQ-selected providers.

III. Joint Presentation Concerning Deferred Compensation Programs

Mr. Greg Johnson, Iowa President, National Association of Insurance and Financial Advisors (NAIFA), and Mr. Richard Dobson, former Iowa Officer, NAIFA, provided a joint presentation to the committee. The NAIFA Iowa representatives noted that there are 1,300 NAIFA members in Iowa. They stated that NAIFA members seek to assist administrators and educators to prepare for their financial future in retirement. The presenters noted that section 403(b) plan participation is a key element of retirement security for Iowa educators, but also noted that only 20 percent of eligible section 403(b) employees currently participate in programs offered by DAS.

The NAIFA presenters stated that the first dollar invested is the most important dollar in retirement planning, given the impact of compounding interest. They then discussed plan contribution limits and opined that thoughtful, learned advice from a professional financial advisor is important for financial planning and taking advantage of investment opportunities. The presenters noted their support for DAS now offering ITQ-selected providers for the section 403(b) plan. Prior to the RIC program, districts offered 250 different investment plans and that since offering eight core provider plans in 2008, the RIC program now offers only four core provider plans. They opined that NAIFA advisors will be able to provide advice to members and increase participation rates among different investor demographics.

In response to a question from Co-chairperson Courtney, the presenters noted that e-mails are not enough to get young people interested in investing, especially while they face other large expenses and lack adequate investing information. Representative Mascher opined that investment decisions might be different across demographics and that an individual's investment portfolio might differ at different stages, noting that young people might be investing in first homes or through private investment options. Senator Danielson later stressed the administrative efficiencies provided under the RIC program, but noted that individuals can find other investment options more attractive than RIC participation, specifically mentioning Roth IRAs, long-term care insurance, and life insurance.

Co-chairperson Pettengill then inquired as to why ITQ-selected plans are only made available to section 403(b) eligible employees and advocated for teaching financial literacy in Iowa schools. The NAIFA representatives noted their support for offering the ITQ-selected plans to section 457-eligible and section 401(a)-eligible employees. The NAIFA representatives provided personal anecdotes related to offering constant plan management for individual plan participants and the rise of investor and agent fatigue with frequent plan changes under the RIC program. The representatives also provided comparative analysis of supplemental retirement investment programs in other states. Representative Carlson responded to the indication of investor fatigue by noting that assets invested under a prior qualifying plan may remain in that plan after it becomes disqualified from the RIC program.

IV. Legislative Services Agency — Pension Overview

Mr. Ed Cook, Senior Legal Counsel, Legislative Services Agency (LSA), noted that the committee has considered many issues over the course of the 20 years that he has served the committee. He stated that Iowa offers six different retirement systems for public sector employees. He discussed how the General Assembly and the Public Retirement Systems Committee provide oversight over the retirement systems, and noted that provisions in the Iowa Code serve as the plan documents for these six retirement systems. He then specifically noted that when the General Assembly makes changes in one system, that individual groups will often seek to make similar changes within the other five systems.

The six systems include three separate programs administered by the Iowa Public Employees' Retirement System (IPERS), programs offered for general employee populations, for protection occupation employees, and for sheriffs and deputies. The other three retirement systems serve judges, peace officers, and police and fire employees in certain cities (the Municipal Fire and Police Retirement System of Iowa pursuant to Iowa Code chapter 411), respectively. In discussing the retirement systems for public safety employees, Mr. Cook noted that those systems offer disability income elements and that members of certain systems do not generally contribute to or receive benefits from Social Security.

Mr. Cook noted that the systems provide retirement benefits for employees, including retirement security through income replacement while providing employers with additional means to attract and retain high-quality employees. He then noted that retirement often works as a three-legged stool, that includes Social Security, pension benefits, and private investment savings; he also noted, however, that members of two Iowa retirement systems do not generally participate in Social Security.

Mr. Cook discussed the funding mechanisms for the retirement systems and the standard system formula that Contributions + Investments = Benefits + Expenses, noting that change to one end of the equation inevitably impacts the other end of the equation. Mr. Cook then discussed the difference between defined benefit (DB) and defined contribution (DC) plans, noting that DB plans essentially serve as insurance policies for retirement with specified benefit limits. He noted that, as in standard insurance plans, the benefit risk is pooled, with some employees receiving greater benefits than others while some employees will bear contribution burdens without receiving commensurate benefits when leaving qualified employment. He stated that the ultimate goal of the systems is to actuarially fund a retiree's benefits during the individual's working life.

Mr. Cook then discussed certain actuarial concepts, such as normal cost and unfunded actuarial liability. He also mentioned LSA's Legislative Guide on pensions, other resources and information on pension proposals, and comparative analyses provided by the National Conference on State Legislatures. He then discussed LSA's mapping resources related to pension systems and the creation of an Internet site on the topic that will be made available in January.

Mr. Cook encouraged members to direct any questions on public retirement systems to himself or Ms. Jen Acton, Senior Fiscal Analyst, LSA.

V. Presentation Concerning the Municipal Fire and Police Retirement System of Iowa (Iowa Code Chapter 411)

Mr. Terry Slattery, Executive Director, Municipal Fire and Police Retirement System of Iowa (411 System), discussed his four years of service with the system as its Executive Director. Mr. Slattery discussed legislation from 1990 creating the system's nine-member board along with four ex officio legislative members. He provided information on the board's recent strategic planning exercise and how the board serves as fiduciaries to the system, with responsibility for the continued sustainability of the system.

Mr. Slattery discussed the work and duties of system employees, and noted that statutory system requirements related to disability benefits are of great importance to members in the fire and police protection occupations. He noted system responsibilities in maintaining tax-exempt status, investment returns, and member communication programs. He also noted the system's hiring of a communications consultant in order to build a more robust communication presence, and to eventually allow the system to survey its members.

Mr. Slattery discussed the system's asset allocations and the system's obligations to meet liabilities on an ongoing basis on 10-year, 30-year, and 50-year time scales. He noted the system's responsibility to meet investment return needs at the lowest possible risk across the system's different asset classes within a diversified investment portfolio. He discussed the system's use of experience studies, conducted every five years, to provide data on meeting and establishing actuarial assumptions.

Mr. Slattery summarized the provisions of the system's Deferred Retirement Option Plan (DROP) program, stating that 50 percent of eligible employees have decided to participate in the program since it was initiated in 2007. He stated that DROP is a cost-neutral program that allows members to defer retirement over a period of time, and requires the member's full retirement following conclusion of the period. He stated that the program provides employers with information on prospective employment needs.

In response to a question from Co-chairperson Pettengill, Mr. Slattery noted that the system complies with federal regulations, but that the system, as a state-governed plan, is exempt from the Employee Income Security Act of 1974 (ERISA) and certain Department of Labor regulations. He further noted that the system has received a favorable determination letter following an IRS evaluation, for conforming with Internal Revenue Code requirements. He noted that another IRS evaluation will not be required again in the foreseeable future.

Senator Schneider inquired as to how the system's investment allocations have changed since the financial crisis. Mr. Slattery explained that the system provides guidelines to its investment managers and requires that investors meet benchmarks, but that investment decisions within those guidelines fall within a manager's discretion. He noted that the system's need for liquidity as a negative cash flow system, but which operates as a mature retirement system, as intended. Mr. Slattery described performance fees in the system's private equities allocation, stating that the fees usually amount to a 1 percent fee on assets under management with 10 percent carried interest. He stated that the system utilizes portfolio managers due to limited system staffing and due to the specialized knowledge among the system's four investment managers. Mr. Slattery confirmed that he would provide the committee with the actual percentage costs to the committee. Mr. Slattery also confirmed the system's asset categories and allocations following an inquiry from Representative Carlson.

Mr. Slattery discussed the system's higher risk private equity investment strategies while also noting higher returns from private market investing when compared to the system's public equity market returns. He noted the system's overall return goal of 7.5 percent. He also discussed the system's investments in the equity and debt of real estate properties as providing income stream and liquidity, stating that the system's real estate portfolio plays an important role in meeting the system's cash flow needs.

Mr. Slattery discussed the system's required medical examination prior to employment, noting that the board recently adopted national standards from fire and police associations, respectively. He stated that the system has come to prefer the national standards over independently set standards. Also with respect to national standards, Mr. Slattery discussed the system's full implementation of Governmental Accounting Standards Board (GASB) statements 67 and 68. Mr. Slattery mentioned the system's use of document imaging systems to digitally image forms and records and to store system documents electronically, noting that the system currently relies on paper documentation and manual filing. Mr. Slattery stated that the digital imaging project would be completed in 2016, and stressed the additional security and member usability that coincide with electronic document storage.

Senator Danielson asked Mr. Slattery to provide the committee spreadsheets related to the systems GASB statement 68 implementation. Senator Danielson also requested that DROP program reporting include disability program information in the future. Senator Danielson noted that the 411 System provides retirement and disability income, and that most 411 System members do not participate in Social Security or Medicare. He stated that although the system is administered at a statewide level, it currently serves local fire and police employees without a state contribution. He also opined that restoring the state contribution to the 411 System would provide direct property tax relief to 411 System participating cities. Co-chairperson Pettengill then noted that 411 System employees do not make contributions to the system, nor receive pension benefits, for overtime hours and that employees in other state retirement systems are required to make such contributions. She stated that the lack of including employee overtime for the 411 System adds up to a significant amount of money.

Mr. Glen Gahan, Actuary, Silverstone Group, discussed the system's funding policy, noting the system's movement to a closed 25-year amortization period at a fixed rate with a level dollar. He stated that the system had an open 25-year amortization period prior to the change. The level-dollar method is more costly initially compared to the percentage-of-pay method, but becomes less costly than the level percentage-of-pay method in subsequent years. Mr. Gahan explained the system's 2007-2008 portfolio losses before noting the system's current $2.3 billion in assets and 81 percent funding ratio. Mr. Gahan stated that the fund is stable and discussed the system's most recent 10-year experience study and the success of the system's recent independent actuarial audit.

Senator Schneider asked why the system had chosen a 25-year closed amortization period, when the Society of Actuaries' Blue Ribbon Panel on Public Pension Plan Funding recently recommended that public pensions adopt 15-to-20-year amortization plans. Mr. Slattery stated that the system made a major change in 2013 when it moved from an open to a closed amortization period. He stated that he believed the 25-year period to be appropriate, based on the length of terms of employment and stated that a 25-year amortization period is both reasonable and sustainable. Mr. Gahan then discussed the impacts of life expectancy and the system's adopted 1994 mortality table. He stated that the system analyzes its assumptions and mortality tables as part of the system's experience studies and in their 10-year evaluations, which the system produces every five years. Mr. Gahan described the system's blended 1994 mortality table as both reasonable and conservative, based on actual experience. He stated that the adopted mortality table matches up most closely to the experience observed in the system's most recent study, but that the system would reevaluate the table again in 2017 during the next experience study.

Mr. Gahan explained the system's investment results and the impacts of the system's five-year actuarial smoothing, noting that the market value of system assets is slightly higher than the current actuarial value as a result of deferred gains, which will likely bolster actuarial value in the coming years. He noted the system's funded ratio is 80.85 percent as of July 1, 2015. Mr. Gahan also discussed the system's 25-year forecast, stating that the funded ratio is expected to increase to 99.12 percent in that period, while city contribution rates are expected to decrease gradually in the coming years.

VI. Iowa League of Cities

Mr. Dustin Miller, General Counsel, Iowa League of Cities, stated that pension issues are a priority for 411 member cities even with contribution rates starting to trend downward. Mr. Miller expressed gratitude for the contributions that fire fighters and police officers provide to member cities, and said that the system is necessary to attract and retain employees. Mr. Miller stated that member cities want to provide a quality pension system and that the cities and employees should not posture themselves as adversaries. He stated a desire among cities to change the tone under renewed dialogue, but noted that some member cities are now making public safety decisions on the basis of cost rather than on actual public safety needs. He stated that these discussions occur within the context of city budgeting processes across the state. Mr. Miller expressed appreciation for the role of the Iowa Code chapter 411 board and the 411 System itself, and suggested that as contribution rates move downward, that changes in the system mortality table can be phased-in without being overly burdensome for cities. He also noted that the shift to a closed amortization period was an important move for the system's sustainability.

Mr. Miller discussed the ongoing cost concerns for cities, stating that the downward trend in city contribution rates does not tell the whole story. He then noted that there are five cities that participate in the 411 System while also making a contribution to Social Security for their employees. Mr. Miller remarked on the discrepancies between short-term disability provisions under Iowa Code chapters 411 and 85 respectively, and stated that the medical costs of the system's new cancer presumption provisions are borne entirely by cities, while a .05 percent increase in employee contributions only covers the administrative costs to the system. Mr. Miller opined that more information on short-term disability costs from the system would be important and useful for any reform proposals. He also advocated for rededicating state funding to the 411 System, saying that state contributions ended in 2013 and expressed hope that the state would recommit itself to its historical 3.79 percent contribution. Mr. Miller also then discussed compliance with, and the varied impacts of, GASB 67 and 68 on member cities within the context of city budgeting decisions. Mr. Miller stated that his organization looks forward to participating in renewed and positive dialogue despite some remaining areas of disagreement between cities and their protection employees.

Representative Koester thanked Mr. Miller for expressing interest in a renewed and positive dialogue. In response to a question from Representative Koester, Mr. Miller noted that the cities of Ankeny, Camanche, and Fairfield are the cities that make both 411 System and Social Security payments for fire and police employees, while the cities of Clive and Evansdale make both payments for police employees alone. Representative Koester advocated for program changes to provide more equitable outcomes for those five cities and Mr. Miller noted that these five cities would like to see the issue addressed. Mr. Miller then discussed workers' compensation case law under Iowa Code chapter 85 and Iowa Code section 411.15 and how the 49 cities within the system address workers' compensation issues, and noting that fire employees are the largest drivers of workers' compensation costs. Mr. Miller noted that the workers' compensation-like pool operated by the Iowa League of Cities for coverage based on Iowa Code section 411.15 offers a unique service to member cities, and that the pool is currently running well.

Representative Mascher commended Mr. Miller for the shift in tone and for the cities' expression of appreciation for the work of their police and fire employees. In response to a question from Representative Mascher, Mr. Miller confirmed that there is limited data on the actual medical costs associated with the system's new cancer presumption and noted difficulties drafting appropriate public information requests to receive such information. Mr. Miller stated that there is no requirement for uniform reporting and opined that more research is needed, especially related to medical costs under the system. Co-chairperson Pettengill and Mr. Miller then discussed relative workers' compensation costs for fire fighters and statistics published by the Iowa Municipal Workers' Compensation Association.

VII. Presentations from Employee Associations Primarily Concerned with Iowa Code Chapter 411

Mr. Doug Neys, President, Iowa Professional Fire Fighters, thanked the committee for their work in supporting a sustainable 411 System and expressed gratitude for the refreshing tone from the Iowa League of Cities, stating that the call for renewed dialogue was appreciated. Mr. Neys expressed support for the state contribution request made by Mr. Miller. Mr. Neys also remarked that improving health and safety is an important part of the relationship between fire employees and cities and that informed conversations are important. Mr. Neys noted that the Iowa Professional Fire Fighters organization is not proposing any system changes during the upcoming legislative session. He stated that the system is operating as intended, and is providing a solid benefit to public safety employees.

Mr. Zach Lewis, President, Iowa State Police Association, also expressed appreciation to members of the committee regarding the system and appreciation for the changed tone of the member cities and their recognition of the dangers of these occupations. Mr. Lewis also noted for the committee's consideration that the employee contribution rate, currently fixed at 9.40 percent, has tripled since the system was created, while the city contribution rate has not been doubled in the same period. Mr. Lewis ended by remarking on the composition of the system's governing board, stating that the balance between four city representatives, four member representatives, and one public member is both positive and purposeful.

VIII. Materials Filed With the Legislative Services Agency

The following materials listed were distributed at or in connection with the meeting and are filed with the Legislative Services Agency. The materials may be accessed from the "Committee Documents" link on the committee's Internet Site: https://www.legis.iowa.gov/committees/meetings/documents?committee=655&ga=ALL

1. DAS — Iowa Retirement Investors' Club.
2. MFPRSI — System Presentation.

4017PC - Day 1