# Minutes

A regular meeting of the Benefits and Actuarial Committee of the VRS Board of Trustees was held on October 17, 2018 in Richmond, Virginia with the following members present:

Wallace G. Harris, Chair
Troilen G. Seward, Vice Chair
O'Kelly McWilliams

Board members present:
Mitchell L. Nason, VRS Chair
William H. Leighty

Also present: Trish Bishop, Rory Badura, Judy Bolt, Ty Bowers, Jeanne Chenault, Michael Cooper, Sara Denson, Andy Feagans, Krystal Groff, Taylor Melton, Angela Payne, Andrea Peeks, Jillian Sherman, Virginia Sowers and Cindy Wilkinson of the VRS Staff; Lauren Axselle and Kimberly Sarte of Joint Legislative Audit and Review Commission; Katie Boyle of the Virginia Association of Counties; Sarah Herzog of the Senate Finance Committee; Bea Snidow of the Virginia Education Association; and Matt Yonz, Alisa Bennett (by phone), Larry Langer, and Brad Wild of Cavanaugh Macdonald Consulting, L.L.C.

The meeting convened at 1:30 p.m.

**Approval of Minutes**

Upon a motion by Ms. Seward, with a second by Mr. Nason, the minutes of the February 7, 2018 meeting were approved.

**2018 Actuarial Valuation Results for Five Statewide Retirement Plans, Group Life Insurance, State and Teacher Retiree Health Insurance Credit, and the Virginia Sickness and Disability Program presented by Cavanaugh Macdonald Consulting, L.L.C.**

Mr. Langer of Cavanaugh Macdonald Consulting, LLC, the VRS plan actuary, presented the June 30, 2018 actuarial valuations for the five statewide retirement plans (Teachers, State Employees, JRS, SPORS, and VaLORS). In addition, Cavanaugh Macdonald presented results of Other Post-Employment Benefit Programs (OPEBS) for the statewide plans, including Health Insurance Credit (HIC), Group Life Insurance (GLI), and the Virginia Sickness and Disability Program (VSDP), which includes self-funded Long-Term Care (LTC). Key points from the presentation include:

- The June 30, 2018 valuations are used for informational purposes (odd year valuations are used for contribution rate setting).

- The market value return for the total fund of 7.5% exceeded the long-term assumed rate of return of 7.0%. The corresponding actuarial value asset return for statewide plans ranged from 8.03% to 8.32% due to smoothing of investment gains/losses observed over the previous five years.
- Funded status on both market and actuarial value basis improved for all pension plans except SPORS.
  - Salary increases in excess of assumed rates caused increases in the unfunded liability of the SPORS plan.
- Employer contribution rates decreased for all pension plans compared to the 2017 valuation.
- The 10-year deferred contributions for the 2010-2012 biennium have been fully repaid for all statewide pension plans with the exception of the Teacher plan. The Teacher plan received an infusion of $193 million in fiscal year 2015 to reduce the balance of its 10-year deferred contributions.

Plan Experience and Demographics:

- Slowing or declining active membership was evident in most of the statewide plans with the exception of the Teacher plan, which increased membership by approximately 0.8% during the year.
- The covered population also showed a below average increase in new retirees, which could signal a trend that members are working longer than we have seen in the past.
- Covered payroll is assumed to increase by 3.0% each year in each of the plans. The Teacher plan, VaLORS, and JRS lagged slightly behind that assumption, while the State plan recorded a 3.4% increase. The SPORS plan saw an increase of 14.7% in covered payroll due to previous legislation that provided compression pay increases.
- The average age at retirement continues to show that members are working longer. Over the last ten years the average age at retirement has increased about four years for State and Teacher retirees and approximately one year for SPORS and VaLORS.

Projected Contributions and Investment Return:

- Benefit of pre-funding is that investment returns on pre-funded assets reduce the employer's long-term contributions.
- Cash flow is the difference between the contributions and benefits and expenses of the fund.
- Cash flows will vary for each plan since all plans have different demographics and maturities.
- Mature plans often have negative cash flows over time, which is considered a normal cycle of pension plans.
- Negative cash flows do not necessarily imply a plan is in trouble, in fact part of the benefit of pre-funding is the investment returns can pay a significant portion of benefit payments.

OPEB Results

- Mr. Langer noted little change with respect to Other Post-Employment Benefit (OPEB) employer contribution rates regarding HIC, VSDP and Group Life Insurance.
- Funded status improved for all of the OPEB plans, though the HIC and Group Life plan continue to have funded ratios of only 8.8% and 49.7%, respectively.

Mr. Nason thanked Mr. Langer for his presentation.

Upon a motion by Mr. Leighty, with a second by Ms. Seward, the Committee recommended to the Board the following action:

**RBA: The Virginia Retirement System Board of Trustees accepts the June 30, 2018 Actuarial Valuations conducted by the VRS plan actuary, Cavanaugh Macdonald Consulting, LLC, for the Five Statewide Retirement Systems, Group Life Insurance, Health Insurance Credit and the Virginia Sickness and Disability Program.**

***Request for Board Action:*** The Board accepts the June 30, 2018 Actuarial Valuations conducted by the VRS plan actuary, Cavanaugh Macdonald Consulting, LLC, for the Five Statewide Retirement Systems, Group Life Insurance, Health Insurance Credit and the Virginia Sickness and Disability Program.

**Information Items**
**Review 2018 Stress Testing and Scenario Analysis Report**

Mr. Badura began his presentation of the results of the VRS Stress Test and Sensitivity Analysis by briefly discussing § 51.1-124.30:1 of the *Code of Virginia* that required VRS to adopt a formal policy to regularly report sensitivity and stress testing to members of the General Assembly. Under the Code, the analyses must include projections of benefit levels, pension costs, and debt reduction under various economic and investment scenarios. The report provides an analysis of the potential impact of various scenarios and hypothetical situations on VRS-administered retirement plans and supports transparency with regard to the future health of the retirement system. The report is based on the results of the June 30, 2017 actuarial valuation and focused on:

- The changing pension environment, including plan maturity and volatility.
- Negative amortization and its impact on long-term funding.
- Risks to long-term funding, including investment volatility, longevity, and membership decline risks.

The report included:

- Investment risk analysis including sensitivity and scenario testing.
- Analysis of mortality and longevity risk.
- Risks associated with current trends in membership and payroll growth.
- Strategies to enhance funding including:
    - Reducing amortization periods for remaining legacy unfunded payments.
    - Considering lump sum contributions such as those used to pay down of 2010-2012 deferred contributions for State and Teacher plans.
    - Avoiding the expansion of benefits while plans remain underfunded.

Key points from the presentation include:

- As roughly two-thirds of benefits are funded by investment income, receiving 100% of the Board certified actuarially determined contributions not only avoids adding liabilities to the plans, but also ensures assets are available timely to be invested and take advantage of compound interest.
- Pension reforms, specifically plan design changes, have reduced the future costs of benefits.

- Pension reforms also introduced risk sharing, which serves to lessen both the employer's longevity risk as well as investment risk.
- VRS statewide retirement plans with large unfunded liabilities will be more sensitive to investment risk than the better funded local retirement plans.
- Significant resources must remain dedicated to addressing the amortization of the legacy unfunded liabilities.
- Decreases in active covered membership in some statewide plans could cause increases in future employer rates as a percentage of a smaller covered payroll.
- Strong investment performance in fiscal year 2017 mitigated some of the impact of the assumption changes resulting in slightly lower contribution requirements for most plans.
- Even while mortality assumptions have already been adjusted to reflect members living longer, new studies suggest additional improvements in mortality are likely, which could increase plan liabilities in coming years.
- Analysis suggests that accelerating the payback of the legacy unfunded liabilities could provide significant long-term savings and better position the statewide plans to weather future volatility in investment returns thereby serving to reduce investment risk.
- Due to strong market returns and movement to fully funding the actuarially determined and Board certified contribution rates, unfunded liabilities have declined and over the last five years the funded status of the plans has improved by approximately 10 percent.

Next stress test report based on 2018 valuations is scheduled for spring of 2019.

**Upcoming Meetings**

The next Benefits and Actuarial Committee meeting is scheduled for November 13, 2018 at 1:00 p.m.

**Adjournment**

There being no further business, Mr. Harris adjourned the meeting at 3:52 p.m.

11/13/2018
Date

Wallace G. Harris
Wallace G. Harris, Chair