MINUTES
of the
THIRD MEETING
of the
INVESTMENTS AND PENSIONS OVERSIGHT COMMITTEE

August 31, 2011
Park North Building Rotunda
Science and Technology Park, University of New Mexico
801 University Blvd. SE
Albuquerque, New Mexico

The third meeting of the Investments and Pensions Oversight Committee (IPOC) for the 2011 interim was called to order by Senator George K. Munoz, chair, on Wednesday, August 31, 2011, at 9:10 a.m. in the Park North Building Rotunda located at the Science and Technology Park at the University of New Mexico (UNM) in Albuquerque, New Mexico.

Present
Sen. George K. Munoz, Chair
Rep. Henry Kiki Saavedra, Vice Chair
Rep. William "Bill" J. Gray
Rep. Larry A. Larrañaga
Sen. Carroll H. Leavell
Sen. Steven P. Neville
Sen. Mary Kay Papen
Rep. Jim R. Trujillo

Absent
Rep. David L. Doyle
Sen. Timothy M. Keller
Sen. John M. Sapien
Rep. Luciano "Lucky" Varela

Advisory Members
Rep. Donald E. Bratton
Rep. Miguel P. Garcia
Rep. Patricia A. Lundstrom
Sen. William H. Payne
Rep. Jane E. Powdrell-Culbert
Rep. William "Bill" R. Rehm
Rep. Sheryl Williams Stapleton
Rep. Mimi Stewart
Rep. Shirley A. Tyler
Sen. Carlos R. Cisneros
Sen. Tim Eichenberg
Rep. Roberto "Bobby" J. Gonzales
Rep. Rhonda S. King
Sen. Stuart Ingle
Sen. John C. Ryan
Sen. Michael S. Sanchez
Sen. John Arthur Smith
Rep. Richard D. Vigil

Staff
Tom Pollard, Legislative Council Service (LCS)
Claudia Armijo, LCS
Doug Carver, LCS

Guests
The guest list is located in the meeting file.

Handouts

Handouts and written testimony are in the meeting file and posted on the New Mexico Legislature web site.

<u>Wednesday, August 31</u>

Senator Munoz welcomed the committee members and guests. He asked members to introduce themselves, which they did. Senator Munoz invited David Harris, executive vice president for administration, chief operating officer and chief financial officer for UNM, to address the members.

Mr. Harris welcomed the committee to the UNM campus on behalf of himself and UNM President David Schmidly, who was unable to attend due to a previous commitment. Mr. Harris reminded members about the various schools within the university complex, including the:

- Anderson Schools of Management;
- College of Arts and Sciences;
- College of Education;
- College of Fine Arts;
- College of Nursing;
- College of Pharmacy;
- School of Architecture and Planning;
- School of Engineering;
- School of Law;
- School of Medicine; and
- School of Public Administration.

Mr. Harris invited and encouraged committee members to explore the entire UNM campus.

Next, Mr. Harris told the members that UNM is a large stakeholder in matters under consideration by both the Educational Retirement Board (ERB) and the IPOC. He noted that in 2010, the university made more than $100 million in contributions to the educational retirement plan, composed of $53 million contributed by the university and $47 million by employees. He also noted that currently, approximately 3,300 former UNM employees are retired and receiving benefits. Mr. Harris introduced Helen Gonzales, vice president of human resources for UNM.

Ms. Gonzales noted that the UNM Human Resources Department maintains a good working relationship with the ERB. She assured members that the university is very interested in maintaining a strong retirement fund for its employees and retirees, as well as a strong continuing relationship with the ERB.

Impact of Various Retirement Benefit Plan Changes on ERB Pension Fund Solvency

Jan Goodwin, executive director, ERB, began her presentation by introducing ERB board members present at the meeting. She asked Mary Lou Cameron, ERB board chair, to address the committee.

Ms. Cameron thanked the committee for inviting the ERB to the meeting and allowing her to speak. She noted that as chair, she can assure the IPOC that each member of the board takes the member's fiduciary responsibility seriously and invests the time and energy needed to accomplish the work of the ERB. She added that the board considers ensuring the long-term sustainability of the members' retirement benefits as one of its primary duties.

Ms. Cameron said that last year, the ERB was recognized for its willingness to step up, as requested by the legislature, to present a plan design change to the IPOC to assure the Educational Retirement Fund's solvency. While that recommended change did not pass the legislative process, the board has continued its work during this calendar year to look at plan design features that will impact current and future members. She explained that the board's goal is to use factual and sound information in looking at potential plan design changes that will sufficiently improve the solvency of the fund in the shortest period of time possible, while providing minimum disruption to the benefits of the maximum number of the members. Ms. Cameron reminded the committee that the members work hard and must plan for an adequate and deserved retirement.

Ms. Cameron further noted that the ERB recognizes that communicating its work to the plan members is a priority if the board hopes to gain support for any recommended changes. The fund serves approximately 130,000 retired, active and inactive members from the state's education community. Those members expect and deserve transparency from the ERB entrusted to protect and preserve their retirement fund. She followed by noting that the legislature deserves the same.

Ms. Cameron followed by telling members that the ERB is aware that it is unrealistic to expect the legislature to increase the state's contribution higher than the 13.9% promised in 2005. At the same time, the board is cognizant that the active members are in a multiyear stagnant period of little or no significant salary increase, as well as an increase in retirement contributions due to the shift in those contributions from the employer to the employee. Retired members are anxious about the negative impact of the flat Consumer Price Index (CPI) on the cost-of-living adjustment (COLA). In 2011, retirees are seeing a decrease in benefits due to an increase in dental insurance rates.

Ms. Cameron closed her discussion by saying again that the ERB remains committed to a working partnership with the legislature to improve the Educational Retirement Fund's solvency and ensure benefits for all members, retirees, active employees and future members. She thanked the committee again and turned the discussion over to Ms. Goodwin to explain the work and processes that the ERB continues to undertake in reaching its solvency goals.

Ms. Goodwin directed the members' attention to the handout provided by the ERB titled "ERB Solvency Considerations" dated August 31, 2011. The handout contains numerous plans that the ERB is considering as potential changes to the plan. Ms. Goodwin began by explaining the status of the fund as of June 30, 2011. She pointed out that prior to the board's decision to change the investment earnings assumption ratio from 8% to 7.75%, the fund's unfunded actuarial asset liability was $4.9 billion. However, due to the change in the investment earnings ratio to 7.75%, the unfunded liability on June 30, 2011 stood at $5.9 billion. The change to the new target investment rate also increased the fund's time period to amortize its unfunded liability from 62.5 years to an infinite date.

Ms. Goodwin next reminded the members that the ERB has set the goal of a funded ratio of 80% within 30 years, which would be in alignment with the Governmental Accounting Standards Board (GASB) Standard 27. Ms. Goodwin reminded the members that on July 8, 2011, the GASB proposed changes in pension accounting and financial reporting standards for state and local governments. She noted that the GASB's stated goals are to improve the visibility and quality of pension information in governmental financial statements and to encourage intergenerational equity. Ms. Goodwin told the members that the ERB, in considering all options and speaking at length with its actuaries, has determined that if only "new" members are affected by plan changes, it will take too long for the changes to make an impact on the solvency of the plan, particularly in light of the GASB changes.

Next, Ms. Goodwin reminded the committee members of the outcome of the phone poll conducted by Research & Polling, Inc., on behalf of the ERB. The purpose of the survey was to find out what, if any, support polled members might have for certain changes to the ERB plan. The survey was conducted in the week beginning October 30, 2010. The ERB staff provided Research & Polling with contact numbers for 400 randomly selected active members. Of those polled, 35% were higher education employees and 65% percent were K-12 employees. The results of the survey indicated that 35% of those polled approved of an increase in member contributions, while only 5% approved a decrease in retirement benefit payments for current employees. Of the members polled, 12% did not approve such changes and 4% did not know or declined to respond, while an additional 3% responded that "it depends". The poll revealed that 41% of those asked approved a combination of increased member contributions and decreased retiree benefits for current employees for the purpose of providing solvency to the Educational Retirement Fund.

In the summary, according to the ERB, members are willing to:

1) increase current member contributions by 0.5%;
2) change the final average salary from five years to seven years;
3) implement a minimum retirement age of 60 years for unreduced benefits;
4) implement increased multipliers with continuing additional years of service; and
5) implement a minimum retirement age of 60 years for members to receive ANY retirement benefits.

ERB members polled are divided on the issues of increasing current members' contributions by 1.0%. She also noted that members polled are not willing to reduce the multiplier for future service, nor are they willing to reduce the COLA for current workers upon their retirement.

Ms. Goodwin advised members that the ERB is working with its actuaries and developing a solvency matrix in its efforts to compare multiple change scenarios. She directed members' attention to the handout, beginning on page 8 and continuing through page 19. These pages detail the specific potential changes for the plan and the outcomes projected to be associated with those changes. Ms. Goodwin was careful to emphasize that the board has not approved any particular change illustrated in the studies. Rather, the board continues to work with its actuaries to explore all possibilities, with a focus on changes that will achieve the greatest improvement for the fund in within the board's desired time frame.

Many committee members expressed the hope that the board will come up with recommendations that can be supported by legislators. Members inquired as to the ERB's plan for stakeholder input regarding potential changes, particularly in light of the fast-approaching 2012 legislative session, and the even faster-approaching end date for the IPOC's work schedule.

Ms. Goodwin assured the members that the ERB plans to reach out to its membership and gain input regarding changes. There are plans to hold meetings in areas throughout the state and allow members to voice their concerns and ideas and ask questions. The ERB intends to narrow its focus and report back to the committee at its next meeting.

Some committee members pointed out that many of the potential changes under consideration by the ERB would involve changes that would cause there to be substantial differences between benefits offered by the ERB plan and the Public Employees Retirement Association (PERA) plan. Members expressed concern about making the plans extremely dissimilar and the perception of the unfairness associated with one plan being less generous to its members.

Members voiced the desire for the ERB and the PERA to consider the New Mexico taxpayers in their deliberative processes regarding changes to the respective plans.

There was confusion regarding the various studies that would make changes to the COLA and to which members those studies might be applicable. Ms. Goodwin explained that some of the studies apply to all members, some to current members and new hires and some to new hires only. When asked how many of the ERB's current membership are non-vested members, Ms. Goodwin responded that there are 2,000 non-vested members as of June 30, 2011, which amounts to roughly one-third of the plan members.

Discussions turned to the two changes that the ERB actuaries have explained will make the biggest impact regarding the unfunded liabilities of the plan: changes to the COLA and the retirement eligibility age.

Committee members discussed the issues related to making changes to the plan for current and vested members. Many pointed out that some of the potential legal issues are unknown. Some committee members wondered, if a current member's service credit and retirement benefits earned to date remain unchanged and all that is changed applies to future earnings, could that type of change help avoid legal entanglements? Members also expressed a desire to uphold promises made to employees, particularly since workers plan for their futures based upon those promises.

Ms. Gonzales, speaking on behalf of the university, told members that, as the representative of the university, UNM is in favor of shoring up the solvency of the fund. However, UNM employees would favor studies that would impact non-vested employees and studies that would implement a minimum retirement age. She strongly encouraged the ERB board members to reach out to members and get their input so as not to catch them off-guard with changes to the plan.

Impact of Return-to-Work Legislation on the Educational Retirement Fund Solvency and Teacher Recruitment

Ms. Goodwin led the discussion of the return-to-work process related to the ERB. She said that there are currently 1,400 employees that have returned to work. To be eligible, a retired ERB member must take one full year off after beginning retirement before that member can return to work. At the point in which they return to employment, they must contribute to the fund, may receive both their pension payment and their salary, but receive no additional service credit. At any point along they way, the employee can suspend the employee's pension and start earning service credit. According to Ms. Goodwin, the ERB actuaries have deemed the current return-to-work process beneficial, not detrimental, to the plan.

Next, the members heard from three return-to-work teachers invited to speak at the meeting. The teachers addressing the members were Mary Boognl, a teacher from the Central Consolidated School District in Kirtland, New Mexico, and Don Mitchell and Joe Macias, teachers from the Gallup-McKinley County School District.

Ms. Boognl, Mr. Mitchell and Mr. Macias spoke against the requirement in the law requiring them to contribute to the retirement fund. Ms. Boognl pleaded for the members to consider the plight of the low-paid teachers dedicated to serving New Mexico's students. She said that it is ill-advised to remove incentives for gifted and dedicated teaching professionals to seek and remain in teaching positions in New Mexico's schools. She explained her path in becoming a teacher and her willingness to forgo higher salaries in lucrative positions that could have utilized her skills, preferring instead to remain in the classroom. She emphasized the need for the public schools to recruit teachers that love the profession and care more about teaching kids than the size of their paychecks. However, she cautioned that the realities of pay are still issues that teachers must face. She feels lucky to be able to pursue her passion for teaching despite the low pay. Mr. Mitchell and Mr. Macias echoed the sentiments of Ms. Boognl, relaying similar personal stories about their desires to teach and impact the lives of their students.

Members thanked the teachers for their dedication to New Mexico's school children and for the teachers' willingness to speak with the committee. Members shared their understanding of the teachers' frustrations regarding pay and the required contributions to the Educational Retirement Fund. However, generally, the members seemed to agree that the ERB was never designed to be more than a retirement fund.

Impact of Various Retirement Benefit Plan Changes on the PERA

Terry Slattery, executive director for the PERA, addressed the committee. He began by introducing the PERA board members present at the meeting. Board member Oscar J. Arevalo told the committee that the PERA board asked the PERA's actuary to change the investment rate from 8% to 7.75%, and then to analyze the fund under the new investment assumption. He noted that the board received a summary of the analysis two days prior to the IPOC meeting. However, he provided copies of the letter with the summary for the committee members' reference.

The results of the analysis completed by the PERA's actuary, Cavanaugh Macdonald Consulting, LLC, were provided in a letter to Mr. Slattery and the PERA board. Mr. Slattery gave committee members copies of the letter as a handout dated August 30, 2011. Pertinent information provided in the letter is noted below.

The analysis reviewed the long-term solvency of the PERA fund. The actuary was careful to note that the analysis is based on current active and retired members of the five divisions within the PERA and does not include the Legislative Division. The type of analysis used is called a "closed group" projection, as it does not explicitly include information regarding the impact of members hired after the measurement date of June 30, 2010. Mr. Slattery stated that a more meaningful analysis would be an "open group" projection that explicitly includes future members as replacements of active members exiting employment in future years and then performs annual valuations for each future year of the projection period. However, time did not permit performing an open group projection and the actuary recommended that such analysis be performed after completion of the PERA's June 30, 2011 actuarial valuations to provide additional and more definitive information on the expected long-term actuarial condition of the PERA.

In the analysis, the actuary compared the PERA's projected solvency under the current plan provisions of each division to the projected solvency assuming the "ideal" as outlined in the handout and introduced as legislation last session. This plan affects only those hired after June 30, 2010.

The actuary assumed that the current statutory contribution rates remain in effect for all future years and that the current contribution shift sunsets after the fiscal year ending in 2013. Additionally, the actuary used the latest information for the market value of assets as of June 30, 2011.

Under the current plan, which includes the recent change to retirement eligibility for those hired on and after July 1, 2010, the closed group projection results in the market value of assets being depleted in 2041. The plan's solvency is extended by eight years (to 2049) with the implementation of the ideal plan.

Mr. Slattery asked the committee members to consider the following.

The state police plan, based on the June 30, 2010 valuation, had a funding surplus of approximately $106 million and remains solvent over the projection period under both the current plan design as well as with the implementation of the ideal plan. Under the implementation of the ideal plan, the municipal general plan remains solvent throughout the 50-year period of the analysis. However, the other three plans (state general, municipal police and municipal fire) are not sufficiently impacted by the implementation of the ideal plan to ensure the long-term solvency of these divisions. These three divisions together represent approximately 65% of the liabilities of the PERA. The degree of reduction to the benefits provided to future members hired after July 1, 2010 would need to be far greater in order for the normal cost attributable to those members to be reduced enough for these divisions to maintain solvency throughout the projection period. If solvency is to be sustained through a change in benefits for future employees only, the resulting benefit design for those employees would likely be in the bottom tier of plans in the country considering the benefits earned in relation to the amounts contributed by the members. Absent such a drastic decrease in benefits for future employees, the sources available to improve solvency must also consider the benefits paid to current members and/or increases in contributions. Considering that the State General Division by itself constitutes nearly 45% of the PERA liabilities, the ideal plan would only increase the period of solvency of the entire fund by four years. The actuary suggests considering application of the COLA provisions of the ideal plan to all current members (active and retired) as the basis for determining the future annual adjustments. Based upon the closed group projections, it would appear that such a change, provided that the CPI is similar to historic levels, would sufficiently reduce the expected benefit payments in order to reestablish long-term solvency for the State General Division. Solvency would be improved for the municipal police and municipal fire plans, but there would still need to be further consideration of additional changes to the benefits provided to future employees and/or increases to contribution rates to reestablish long-term solvency.

In closing, the actuary noted that the full open group projections that are scheduled to follow the delivery of the 2011 valuation reports will provide better information on the projected valuation results for the next 50 years, as well as the expected cash flow and long-term solvency. It would also be better to assess further changes to be considered.

Mr. Slattery told members that the PERA will receive its next valuation from the actuary in October 2011. He also told the committee that the PERA board hopes the ideal plan recommended by the board will be introduced as legislation during the upcoming 30-day session. Both Mr. Slattery and Mr. Arevalo emphasized that the board had only received the analysis from its actuary one day before the meeting. They asked for time to review it and make further recommendations.

There was a general discussion regarding the ideal plan. Members asked to be reminded regarding the concepts and changes proposed in the ideal plan. The discussion continued with committee members asking what additional changes the board is reviewing. Mr. Arevalo noted that making changes to vested members is still "on the table".

The chair reminded the PERA and the ERB boards that the committee hopes to review legislative proposals at the next meeting. He added that the boards need to have plans for solvency. With no further business, the meeting adjourned at 3:55 p.m.