MINUTES OF THE
ADVISORY COMMITTEE ON BENEFIT DESIGN
OF THE BOARD OF TRUSTEES OF THE
TEXAS MUNICIPAL RETIREMENT SYSTEM

On August 18, 2016, the Advisory Committee on Benefit Design (the Committee) of the Board of Trustees (Board) of the Texas Municipal Retirement System (TMRS) convened for a meeting at 8:35 a.m. at TMRS Headquarters, located at 1200 North IH 35, Austin, Texas. The following members were present:

Advisory Committee Members

Bill Philibert, TMRS Trustee and Committee Chair
Roy Rodriguez, TMRS Trustee and Committee Vice-Chair
Alex Cramer, Arlington Professional Fire Fighters (APPF)
Keith Dagen, Government Finance Officers Association of Texas (GFOAT)
Michael Dane, Assistant City Manager, City of San Angelo
Bryan Langley, Assistant City Manager, CFO, City of Denton
Heidi Manti, Service Employees International Union (SEIU, Alternate)
Julie Masters, Mayor, City of Dickinson
Tadd Phillips, Texas Municipal Human Resources Association (TMHRA)
David Riggs, Texas State Association of Fire Fighters (TSAFF, Alternate)
J.J. Rocha, Texas Municipal League (TML)
David Russell, Texas Municipal Police Association (TMPA)
Greg Shipley, Combined Law Enforcement Associations of Texas (CLEAT)
Lori Steward, City of San Antonio
Greg Vick, Texas City Management Association (TCMA)
Charles Windwehen, Retiree

The following staff, consultants and guests were also present:

David Landis, TMRS Trustee
David Gavia, TMRS Executive Director
Eric Davis, TMRS Deputy Executive Director
Christine Sweeney, TMRS General Counsel
T.J. Carlson, TMRS Chief Investment Officer
Leslee Hardy, TMRS Director of Actuarial Services
Dan Wattles, TMRS Director of Governmental Relations
Debbie Munoz, TMRS Director of Member Services
Bill Wallace, TMRS Director of Communications
Rhonda Covarrubias, TMRS Director of Finance
Sandra Vice, TMRS Director of Internal Audit
Michelle Mellon-Werch, TMRS Assistant General Counsel
Ariel Chou, TMRS Actuarial Analyst
Tish Root, TMRS Legal Assistant
Stacy White, TMRS Executive Assistant
Amy McDuffee, Aon Hewitt
Mark Randall, Gabriel, Roeder, Smith & Company (GRS)

Joe Newton, Gabriel, Roeder, Smith & Company (GRS)
Mike Finley, City of Arlington
George Kauffman, City of Garland
Bonita Hall, Texas Municipal Human Resources Association (TMHRA, Alternate)

Mr. Philibert called the meeting to order at 8:35 a.m.

1. **Welcome and Introduction** – Mr. Philibert welcomed the attendees and Ms. McDuffee had those at the table introduce themselves. Guests in the audience were recognized, including David Landis, TMRS Trustee.

2. **Consideration and Approval of June Advisory Committee Meeting Minutes**
Julie Masters made a motion that the Advisory Committee adopt the minutes from the June 23, 2016 Meeting of the Advisory Committee on Benefit Design. Bryan Langley and David Riggs seconded the motion; which passed unanimously.

3. **Review of Agenda and Desired Outcomes**
Mr. Philibert turned the meeting over to Ms. McDuffee. She reviewed the agenda for this meeting and outlined the expected outcome of the discussion: a list of advantages and disadvantages, communication of that list to the Board, and communication regarding the issues back to the constituencies represented by the Committee members. She next reviewed the progress to date and laid the ground rules for optimal progress during this meeting.

4. **Quick Recap of Study Topics**
The Chair delineated the Board's reasoning for assigning these two topics to the Committee.

   a. Return to Work – Joe Newton reviewed the current return to work (RTW) provisions included in the TMRS Act. He reviewed the IRS requirement that there be a bone fide separation from service. While the IRS has not specified specific time frames, it appears that the IRS would find a bona-fide separation period to be at least one year. With a one-year separation, there would likely be no real effect on contribution rates. If the separation period is shorter, there could be increased costs. If changes are enacted that increased retirement behavior by 20%, the average city contribution rate increase would be by 0.03% to 0.13%.

   Mr. Newton next discussed who could be affected by any proposed changes: 1) future retirees only; 2) current retirees who have not returned to work, or 3) retirees who have returned to work but not yet retired again. For the options that include only future retirees, Mr. Newton stated that there is low to no cost for cities, with a small loss of future gain. If current retirees are included who have not yet returned to work, the impact would also be very low to no cost with a loss of future gain (from suspension of annuities). The broader the net is cast, the greater the potential cost increase. Mr. Newton discussed considerations that should apply to all scenarios. Mr. Newton stated that GRS recommends no change in treatment for new accruals, meaning that a new account is created when a member returns to work.

Mr. Newton next discussed the proposed RTW options in lieu of the current provisions:

Option 1: Treat RTW retirees at the last employing city, after a one year break in service, like a member who returns to work for a different city. This option would not suspend the annuity. This is the least complicated administratively, and gives all employers an equal hiring position after a separation period of one year.

Option 2: Decrease the 8-year requirement to one year. In this scenario, the annuity is suspended, but accumulated suspended payments are paid to the retiree at subsequent retirement. There are several possible variants to Option 2 including alternative approaches regarding the accumulated payments suspended during re-employment. Mr. Newton worked through examples of how the various options would work with regard to payment to the retirees.

b. Mr. Newton next reviewed the current COLA options in the TMRS Act, how they are calculated and the funding method. He emphasized the retroactive nature of the current COLA feature. He presented a comparative analysis of an Ad Hoc COLA at 70% of CPI, both with and without the retroactive feature. He next presented the same analysis for a COLA granted on an annually repeating basis. Through discussion, Mr. Riggs suggested, instead of a flat rate COLA option, just offer 100% of CPI as an additional option. Mr. Newton answered questions from the committee on the costs and features of the options presented. Mr. Newton mentioned that in order for a plan to avoid any IRS 415 issues, the accrued benefit must stay below current inflation rates. Mr. Newton then presented one final example of a city that had never adopted a COLA. The main point of the discussion was to demonstrate that the retroactive feature makes the COLA more expensive.

5. **<u>Discussion of Member Requests from June Meeting</u>**

Mr. Wattles began the presentation by providing information requested by the Committee members on various COLA provisions offered by the other statewide systems in Texas. He explained how COLAs work under the Teacher Retirement System (TRS) and the Employees Retirement System (ERS), but noted that due to political and funding issues, TRS and ERS have no regularly occurring COLAs. TRS and ERS have statutory limitations, which require their plans to have an amortization period of less than 31 years before benefit improvements, including COLAs, can be considered. Under the current status of both plans, a COLA would require legislative funding and approval. . With regard to TCDRS, their plan has two types of COLAs, a CPI-based COLA and a fixed rate COLA, both of which are adopted on an ad hoc basis by the individual employers in the system. TCDRS has reported decreased usage of the COLA option in recent years.

In response to a question from the Committee as to whether other plans nationwide have a retroactive COLA feature, Mr. Wattles contacted Keith Brainard, National Association of State Retirement Administrators (NASRA), who confirmed that they are unaware of other systems having a retroactive feature. Alex Brown who also works for NASRA confirmed Mr. Brainard's assertion.

In response to another Committee question, Mr. Wattles stated that 310 of the 850 cities within TMRS have never adopted a COLA. The committee discussed the number of retirees/members this represents. Eric Davis stated that 20%-30% of annuitants are not covered by a COLA. Mr. Wattles stated that in 2016, 45,000 annuitants were covered by a COLA.

Mr. Wattles next discussed the RTW follow-up requests. He stated that Leslee Hardy conducted phone surveys of cities where retirees had returned to work. The responses were presented in the Committee's materials. In response to a question from Mr. Vick regarding age at retirement, Ms. Hardy responded that in those cities surveyed, the average age at retirement was mid-50s, and added that the reasons for retirement may be more personally related.

Mr. Cramer asked what the impetus was for the RTW review. David Gavia stated that there have been return to work bills filed in the past legislative sessions and the one that did change the TMRS plan in 2011 established the 8 year break in service exception. The Board wanted to be more informed and gauge the interest in changes to the provisions from stakeholders in preparation for the next legislative session. Mr. Rodriguez also outlined why the Board wanted to drive the discussion rather than simply react when a bill is filed from another source. He understands the Committee's concerns, but he would rather be proactive and not just reactive on the issues so that when an issue is raised, there has been thoughtful review and the Board can respond. Bryan Langley stated that the 8 year RTW gap is odd and seems arbitrary and said he would like a more equitable solution.

Mr. Riggs brought the discussion back to COLAs, stating that he was shocked no other systems across the country had a retroactive COLA. Joe Newton explained that there are not many agent plans, so you want to have options available to the individual employers while maintaining the stability and security of the system.

Mr. Philibert called for a 15-minute break at 10:08 a.m.
Charles Windwehen spoke on behalf of retirees stating it would be a great help to communities to be able to hire well qualified retirees. He added that the 20-25 year retirement options were based on high stress positions, such as police and fire, but many of these individuals have skills that can continue to benefit the cities they work for.

6. **Presentation and Refinement of a List of Advantages and Disadvantages for Each Return to Work Option Based Upon Advisory Committee Survey Results**

Ms. McDuffee began by reviewing the summarized advantages and disadvantages.

The discussion began with RTW – Option 1, which includes a 1-year break in service, and does not suspend the benefit, but treats an employee the same as if he/she were returning to work at a city other than the last-employing city. The retiree continues to receive his/her benefit payments and his/her salary while employed. She asked for any feedback on the list and observations or questions.

Mr. Vick asked if this option would have a cost impact. Mr. Newton stated that the economic effect of return to work is minimal, although many may still see this as "double dipping". Mr. Vick asked for clarification on item "P" regarding the COLA and clarification on the "double dipping" items, "R" and "S". The committee discussed the perception of double dipping and the factual nature of benefits. The committee discussed the need to be prepared for that characterization of a change for this benefit. The issue of local control was discussed with regard to other policy issues such as transportation, education, and tax caps. Mr. Langley suggested that TMRS may be able to include this in a cleanup bill as a modernization of the System. Mr. Dane said that if there is such consensus on this feature, how TMRS can best move forward to consider implementing a proposal.

Ms. Steward asked if "H" and "O" should be on the list, in that they focus on the individual rather than the System. Mr. Riggs agreed with Ms. Steward that it may be best to reword these to be more neutral to present a more united theme, not just bits from various surveys. She noted her agreement with "C".

Mr. Rodriguez asked for rewording on item "B" to clarify the unfairness issue.

Ms. Masters asked how TMRS benefits work with respect to the increasing longevity of employees. Mr. Gavia explained the changes to mortality tables take into account longer lives of retirees and beneficiaries.

Mr. Wattles added another disadvantage as "bigger risk of changing retirement patterns"

The discussion then turned to the Return to Work – Option 2, after a 1-year break in service, the retiree could return to work at the last-employing city, have his/her annuity suspended but have his/her annuity, including any COLAs granted during the period of suspension, held and paid as a lump sum payment, with or without interest, or re-annuitized upon his/her re-retirement.

Mr. Phillips stated that "D" doesn't make sense to him; why is it listed as a disadvantage of the current System? He also suggested changing the wording in "F" from "Removes" to "Reduces". Mr. Rodriguez suggested removing "F" as it is not an issue for the System and is an earned benefit. Mr. Phillips stated that there is nothing in the disadvantages column that this is a loss of an earned benefit. Mr. Dagen stated that Option 2, "K" is less retiree-friendly, and has less of a possibility to affect retirement trends.

There were other additional concerns regarding Return to Work which include: Should the retiree being made whole refer to whether interest should be paid? The sentiment was "yes" regarding the suspended payments, but not on the interest portion. Mr. Dane stated that retirees forfeit annuity payments when their annuity is suspended. Mr. Dagen and Mr. Langley agreed with Mr. Dane. Mr. Dane stated he is open to a prospective approach, but not for those who are already suspended and have accepted that status, but would be in favor of a prospective approach to un-suspend current working retirees whose annuities are suspended, if there is a way to do it equitably. There was no real Committee disagreement on this part of the discussion.

7. **Presentation and Refinement of a List of Advantages and Disadvantages for Each COLA Option Based upon Advisory Committee Survey Results**

Option 1 – Allows cities to adopt a COLA (either ad hoc or repeating) at 30%, 50%, or 70% of CPI-based only on the change in the CPI in the most recent year. In other words, allow a city to adopt a COLA that does not include the catch-up feature.
The committee reviewed the list of advantages and disadvantages. Mr. Newton stated that "H" is not true. The committee discussed how this option will work and clarified H to say: "For cities already with a repeating COLA there will be no change." Mr. Cramer stated that he would like to add a disadvantage that it could be easier to opt in or out: "B" and "I" both address this. The committee then discussed that while there is no change actuarially, the cities will have more options but the benefit will be less secure. Mr. Vick stated that the majority of cities have been using repeating COLAs for a long time. Is there a motivation for cities that have been paying repeating COLAs to drop to ad hoc? Mr. Newton stated that he doesn't believe there is an incentive to drop to ad hoc if one has been given on a regular basis. It has been harder for cities to drop down from 70% repeating COLAs to 50% because some retirees won't see a COLA for years. Mr. Vick agreed this is a good option for a city as an interim measure when times get tough and they want to decrease COLAs but still give something to retirees.
Mr. Dane shared his concerns with security for retiree benefits in the future. He does not want future councils to be able to reduce benefits for retirees more easily. The committee discussed the difficulties with creating a guaranteed COLA. Mr. Rodriguez clarified that a city council can never decrease a retiree's annuity; it can only limit the amount it increases.
Option 2 – Allow cities to adopt a COLA (either ad hoc or repeating) at a flat rate based on a percentage of the retiree's annuity. In other words, a COLA not tied to the CPI change, 5% for example, subject to IRS limitations. By definition, a flat rate COLA does not have a catch-up feature.
The Committee discussed this provision and the limits on this fixed rate COLA. For example TCDRS has some limitations. Ms. Sweeney mentioned that the way TCDRS is limited is likely based on IRS limitations. She would like to see an adjustment to the description to clarify the limitations. Mr. Langley prefers the variables that are tied to

CPI; they are clearer and limit options. Mr. Gavia explained that for any COLA adoption, the percentage is selected by a city based on available options. TMRS could do calculations to ensure that this does exceed the percentage allowed by the IRS. There was a discussion over how the flat rate COLA would work and be limited. The limit would be set at the rate of a 70% CPI retroactive COLA. Mr. Riggs stated that flat rate colas would be extremely difficult to explain at the legislature. He is extremely opposed to trying to create a new flat rate COLA through legislative action. Mr. Dane feels that the terminology is not a flat rate; he feels that this could be termed a flexible capped percentage COLA. Mr. Windwehen feels that "H" has "unintended consequences" and is too vague. He would like more clarification on this disadvantage. Mr. Phillips would like to add disadvantage that Option 2 is addressing a feature that isn't broken. There are plenty of options and the issue people have is with the retroactivity, not the options available. Ms. Steward would like to have more flexibility.

Mr. Dagan requested to change the wording in "G" from "salary" adjustment to "annuity" adjustment. Mr. Vick has faith that the Board will understand the issues, and that these aren't too negative. Mr. Cramer asked about a window for those that are not currently offering repeating COLAs so that they could get relief from the retroactive provision. Mr. Wattles responded that administratively this is difficult. David Gavia explained for the Committee that in the past we had discussed having a window where we would have one of these options solely for a window period. Mr. Cramer would like to see some way to encourage cities to move toward recurring retroactive COLAs. Mr. Langley stated that there is nothing that currently prevents a council from removing a COLA or decreasing the level of a COLA. He doesn't see any reason to change the current options.

8. **<u>Review of Session and Next Steps</u>**

Ms. McDuffee stated that she will revise the lists of advantages and disadvantages with TMRS staff. The summary of this meeting, along with input of Committee members, will be provided to the Board at the September Board meeting. Mr. Vick said that he sees there is a difficult political climate for pension systems both statewide and locally, and anything that goes forward will need to be very conservative when it comes to behavior and contribution rates. Mr. Dane is not in agreement with the term "negative retirement behavior;" everyone has a right to retire when they reach eligibility. Overall, the Committee agreed to support only those options that do not cause an increase in contribution rates or negatively affect retirement behavior.

Ms. McDuffee and Mr. Philibert thanked everyone for their input and expressed their appreciation for all of the perspectives and knowledge that each member brings to the meeting. Mr. Rodriguez stated that he is very impressed with the level of knowledge and understanding of all of the Committee members on these issues. He stated that TMRS needs their voices across the State and in their communities and constituencies to help people understand TMRS. We hope each community understands that they have the options to elect how they want a plan that benefits them. He also stated that if the Board decides not to introduce a bill, it is likely another entity will and this forum has given the Board a better understanding and insight. Mr. Gavia also thanked the Committee for their participation and time.

9. Public Comment

There was no public comment.

10. Adjourn

Mr. Philibert adjourned the meeting at 12:05 p.m.

David Gavia
Executive Director

David Landis
Chair