

An Introduction to the Retirement Systems of Alabama

Meeting of the Joint Committee on Alabama Public Pensions

October 5, 2015



What Is RSA?

TRS and ERS are statutorily-created state instrumentalities with corporate powers that administer:

- ◆ The defined benefit pension plans for teachers (TRS), state employees and local units (ERS) and judges (JRF);
- ◆ A voluntary deferred compensation plan for government employees (RSA-1); and
- ◆ Numerous other state funds.

Why is RSA different from Private Sector Retirement Plans?

TRS and ERS are *governmental* defined benefit plans.

- ◆ Public pension members' benefits are protected by U.S. and Ala. Constitutions and cannot be changed once employment begins.
 - Legislatures that have enacted certain benefit changes for **current** employees have faced protracted and successful legal challenges.
 - By contrast, private employers may modify future benefits for **current** DB plan participants at any time.
- ◆ ERISA (Employee Retirement Income Security Act) and FASB (Financial Accounting Standards Board) do not apply to governmental plans.
- ◆ ERISA's stringent funding and other requirements and FASB's accounting rules are responsible in large part for the decline in DB plans in the private sector.



Retirement Systems of Alabama Financial *Fast Facts* 2014

For complete 2014 financial statements please see the annual report found at rsa-al.gov

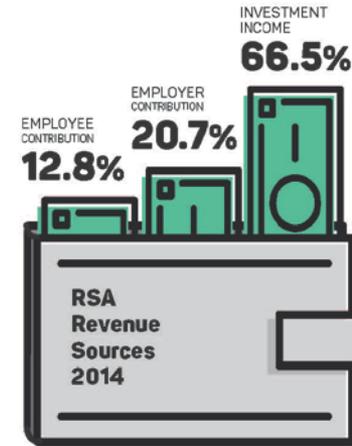
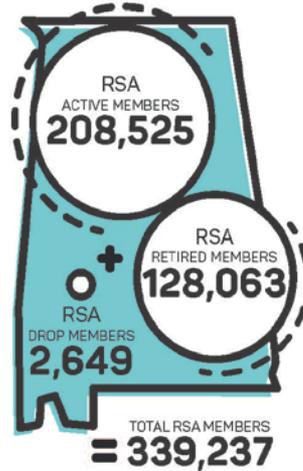
RSA's net earnings of
**\$3.7
BILLION**
are more than

2X

Alabama's General Fund of
**\$1.75
BILLION**



RSA: 2014 Snapshot



Investment Costs

The cost of the average public pension fund is 47 basis points, while RSA's is only 2—the lowest in the industry.



Who Are RSA's Participating Employers?

TRS

13 Universities

27 Post-Secondary

138 Boards of Education

31 State Agencies/Other

ERS State

State of Alabama

ERS Local

292 Cities

65 Counties

513 Other Public Entities

JRF

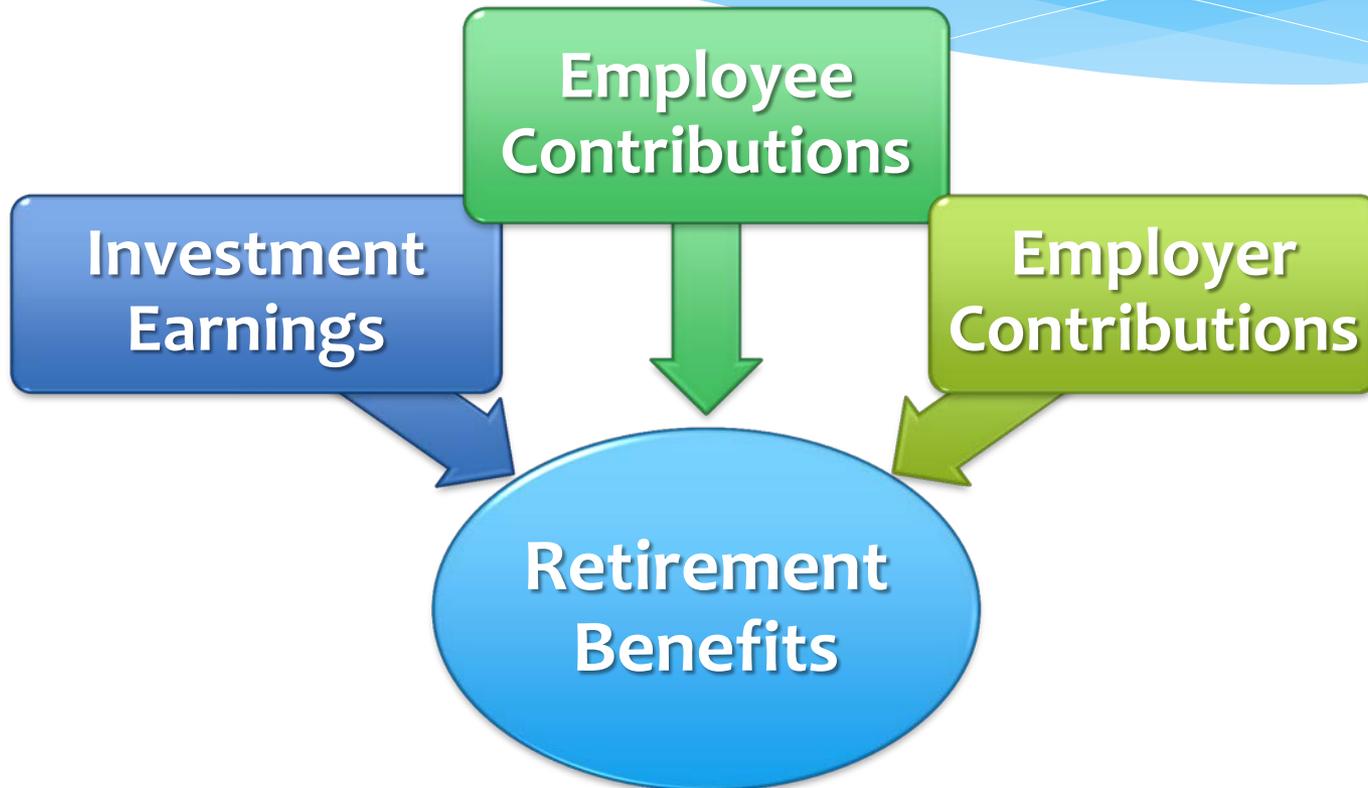
67 Counties (Probate Judges)

AOC (Judges)

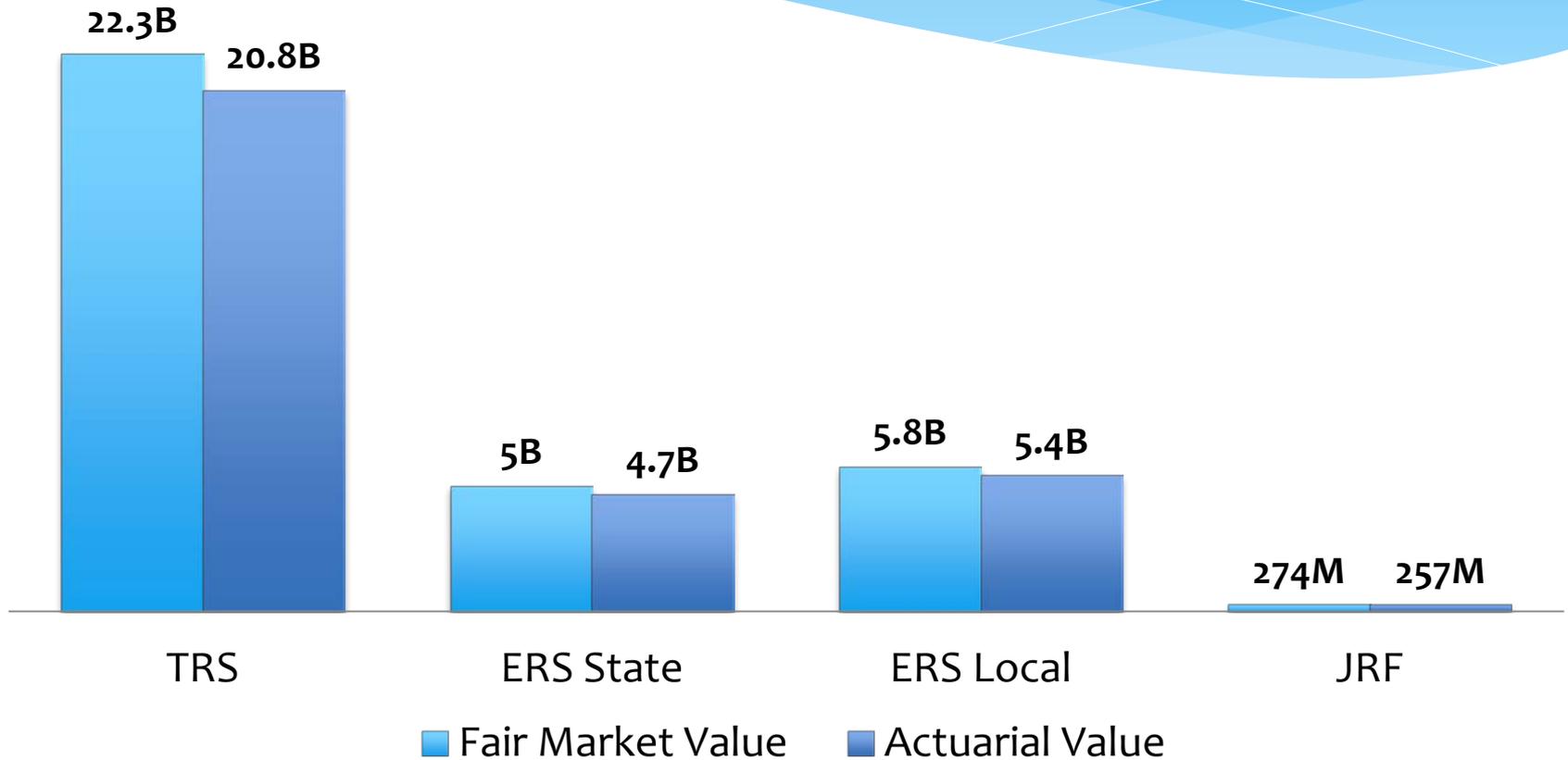
Who Are RSA's Members?

(As of 9/30/14)	TRS	ERS State	ERS Local
Active and Retired Members	222,187	53,276	76,693
Annual Benefits Paid	\$1.9B	\$526M	\$404M
Average Annual Benefit	\$22,169	\$21,410	\$18,637

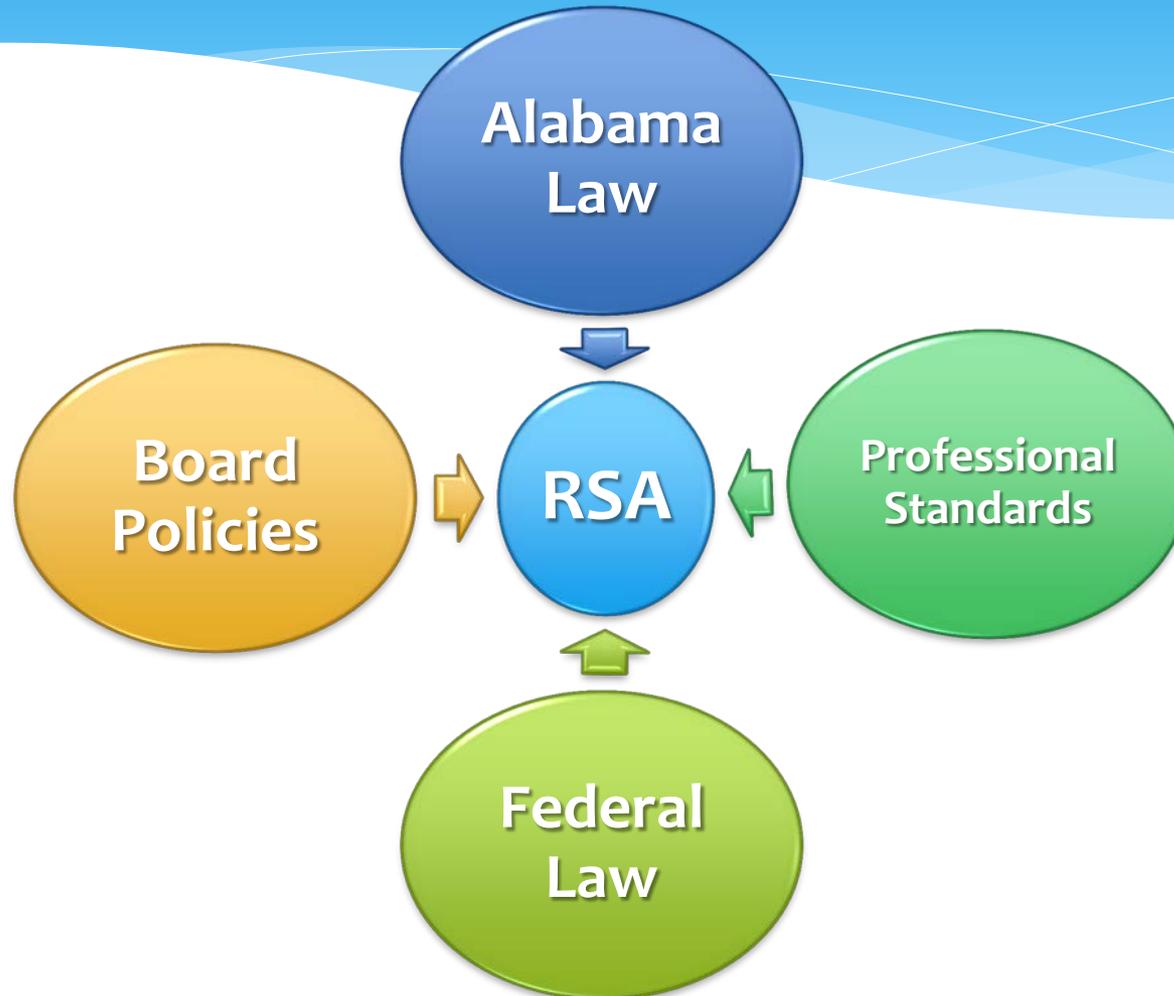
How Is RSA Funded?



Funding Levels as of 9/30/14



RSA Governance



RSA Governance*

◆ Alabama Law:

- Constitutional Provisions
- Governing Statutes and Other Applicable State Laws
 - Ethics Laws
- Fiduciary Duties and Responsibilities to Members
 - Constitutional, Statutory and Decisional Law
 - Prudent Man Rule
 - Duty of Loyalty

*This list is not exhaustive.

RSA Governance*

◆ Federal Law:

- SEC Reporting Requirements, Rules and Regulations
- IRS Rules for Qualified Governmental Plans

◆ Board of Control Policies:

- Investment policy governs the investment activities of the plans
- Funding policy governs

◆ Professional Standards:

- Governmental Accounting Standards Board (GASB)
- Generally Accepted Accounting Principles (GAAP)
- Actuarial Standards of Practice (ASOP)

* This list is not exhaustive.

RSA Accountability and Oversight

Independent Audits:

- ◆ Independent **financial audits** by national certified public accounting firm Carr, Riggs, and Ingram of TRS's and ERS's Annual Financial Statements in accordance with GAAP and GASB.
- ◆ Independent **legal compliance audit** by Alabama Examiners of Public Accounts.
- ◆ SOC 1, Type 2 **audit on effectiveness of controls** by national certified public accounting firm A-lign.

RSA Accountability and Oversight

Valuations/Appraisals:

- ◆ Third-party custodian (State Street) investment returns calculations and portfolio allocation comparisons in compliance with Global Accounting and CFA standards.
- ◆ Independent valuations of private placements by Houlihan Lokey in compliance with applicable valuation standards.
- ◆ Independent valuations of real estate by national appraisal firm Pearson, Inc.
- ◆ Peer reviews of actuarial methodology and experience study.

RSA Financial Transparency

Open Meetings Act

- ◆ Applies to all board and committee meetings

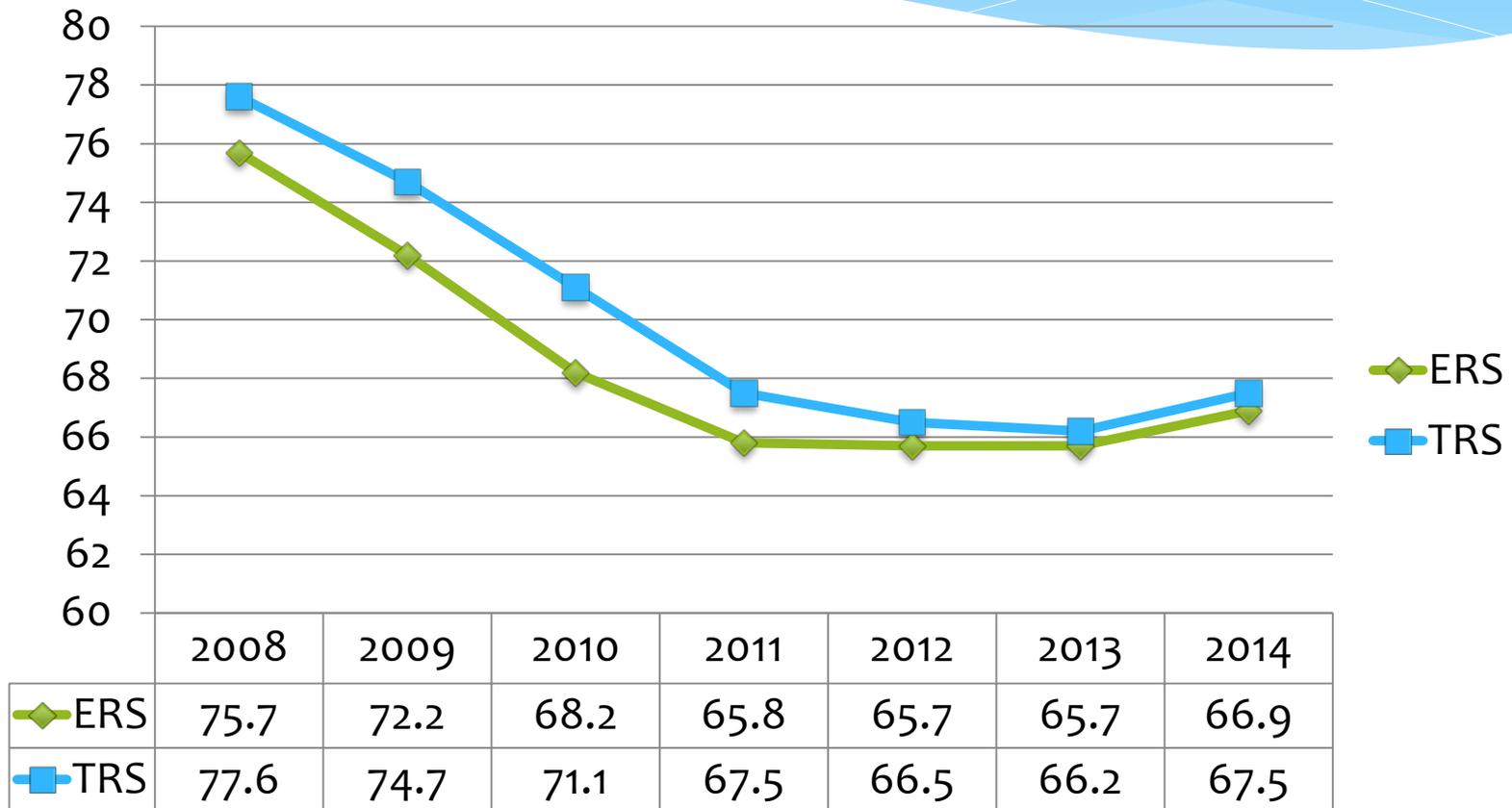
Public Records Act

- ◆ All board minutes, agendas, and documents
- ◆ State Street asset allocation comparisons and investment returns, specifically including the individual private placement and real estate returns.
- ◆ Comprehensive listing of all investments held.

Accessible on Website

- ◆ Comprehensive Annual Financial Report
- ◆ Actuarial Valuations
- ◆ Annual Report
- ◆ Investment Policies
- ◆ Asset Allocations
- ◆ Investment Return Summary

Where RSA's Been: Funded Ratio from 2008-2014



Where RSA's Been: Reasons for Decline in Funding Ratio

◆ Market Meltdowns and Recessions of 2001-2 and 2008-9.

◆ Unfunded Retiree COLAs

- Have paid almost **\$6 BILLION** in unfunded COLA benefits since 1973.
- The present value of all future COLA payments is approximately **\$2 BILLION**.

◆ Open Amortization Schedule

- Refinanced the unfunded liability every year.
- Resulted in large increase in the unfunded liability after 2008-9 market declines and “Great Recession.”

What Has Turned It Around...

◆ Bull Market and High Investment Returns

- Average annualized returns of almost **11%** for past five years

◆ No Unfunded COLAs Passed by Legislature Since 2006

◆ TRS and ERS Boards Amended Funding Policy to Close Amortization Schedules

◆ In-House Investing Currently Saves an Estimated **\$160M** Annually Over Average Investment Costs for Public Pension Plans

◆ 2011-2012 Legislative Pension Reform

- Significantly reduced benefits for employees hired after January 1, 2013 and reduced costs for public employers.
 - ◆ Higher retirement age
 - ◆ No 25 year retirement
 - ◆ Lower benefit multiplier
 - ◆ Abolished DROP
 - ◆ Shifted costs to public employees by raising contribution rates

Results of Reforms To Date

Improved Actuarial Funding Ratio in 2014

- ◆ Increased from **65.7% to 66.9%** for ERS (state and local)
- ◆ Increased from **66.2% to 67.5%** for TRS
- ◆ Market valuation is currently greater than actuarial valuation with smoothed market gains yet to be realized.

Pension Reform=Lower Normal Cost/Lower Risk

- ◆ Number of Tier II employees is rising:
 - 11% of TRS current active employees
 - 12% of state ERS current active employees.
- ◆ Reforms projected to save over **\$4 billion** over the next 30 years.
- ◆ Although savings increase with growth of Tier II, reforms already have saved approximately **\$20.2 million** in employer contributions and benefit costs since January 1, 2013 .

What to Expect from the Experts: Research Director Keith Brainard

Public Pension Expert, Research Director of NASRA (National Association of State Retirement Administrators)

- ◆ Overview of the state of public retirement systems nationwide
 - Key trends and funding levels
 - Is there a pension crisis?
 - Pension reform
- ◆ Discussion of alternative public retirement plans.
 - Plan design
 - How does Alabama compare?

What to Expect from the Experts: Chief Actuary Ed Macdonald

Chief Actuary for Cavanaugh Macdonald

- ◆ Introduction to Cavanaugh Macdonald
- ◆ General Observations
- ◆ Historical Trend Information
- ◆ Valuation Results and Contribution Rates
- ◆ Projection of Funded Ratios
- ◆ Discussion of the costs of alternative retirement plans

What to Expect from the Experts: Chief Investment Officer Marc Green

Chief Investment Officer for RSA, CFA and MBA with 23 years of investment experience

- ◆ Explanation of RSA statutory scheme, investment processes, and controls
- ◆ Introduction to RSA's investment staff
 - Qualifications and credentials
 - Organization and division of responsibilities
- ◆ Discussion of third party custodian's investment returns and asset allocation reports
- ◆ Historic investment returns

Key Documents for Today's Presentations

- ◆ Comprehensive Annual Financial Report, **Introduction 27-174.**
- ◆ Board Funding Policies, **Funding 11-17.**
- ◆ Funding Policy Projections, **Funding 19-20.**
- ◆ Actuarial Valuations, **Funding 21-124.**
- ◆ Investment Policy Statements, **Investments 11-26.**
- ◆ Investment Return Reports, **Investments 27-43.**
- ◆ Pension Reform Projections, **Pension Reform 7-8.**