

# 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

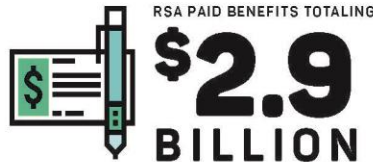
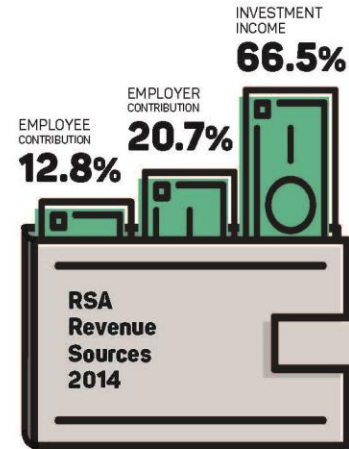
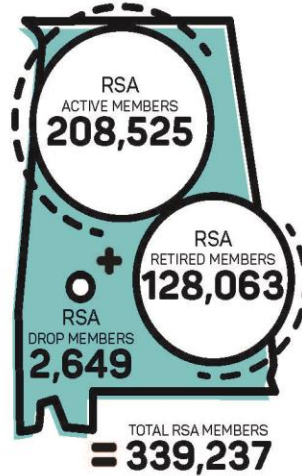
For complete 2014 financial statements please see the annual report found at [rsa-al.gov](http://rsa-al.gov)

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

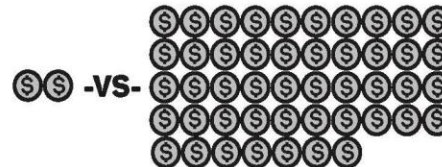


Alabama's General Fund of  
**\$1.75  
BILLION**

# 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

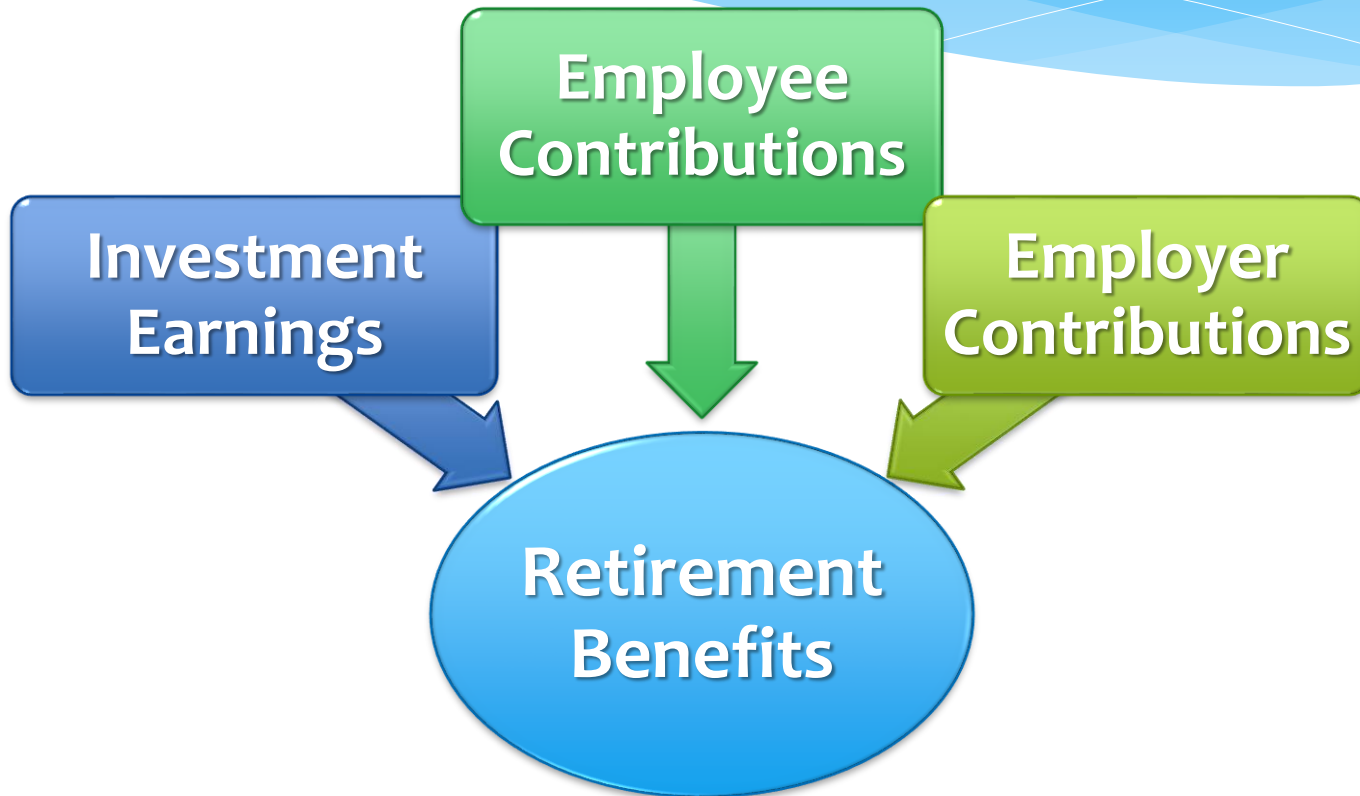
67 Counties (Probate Judges)

AOC (Judges)

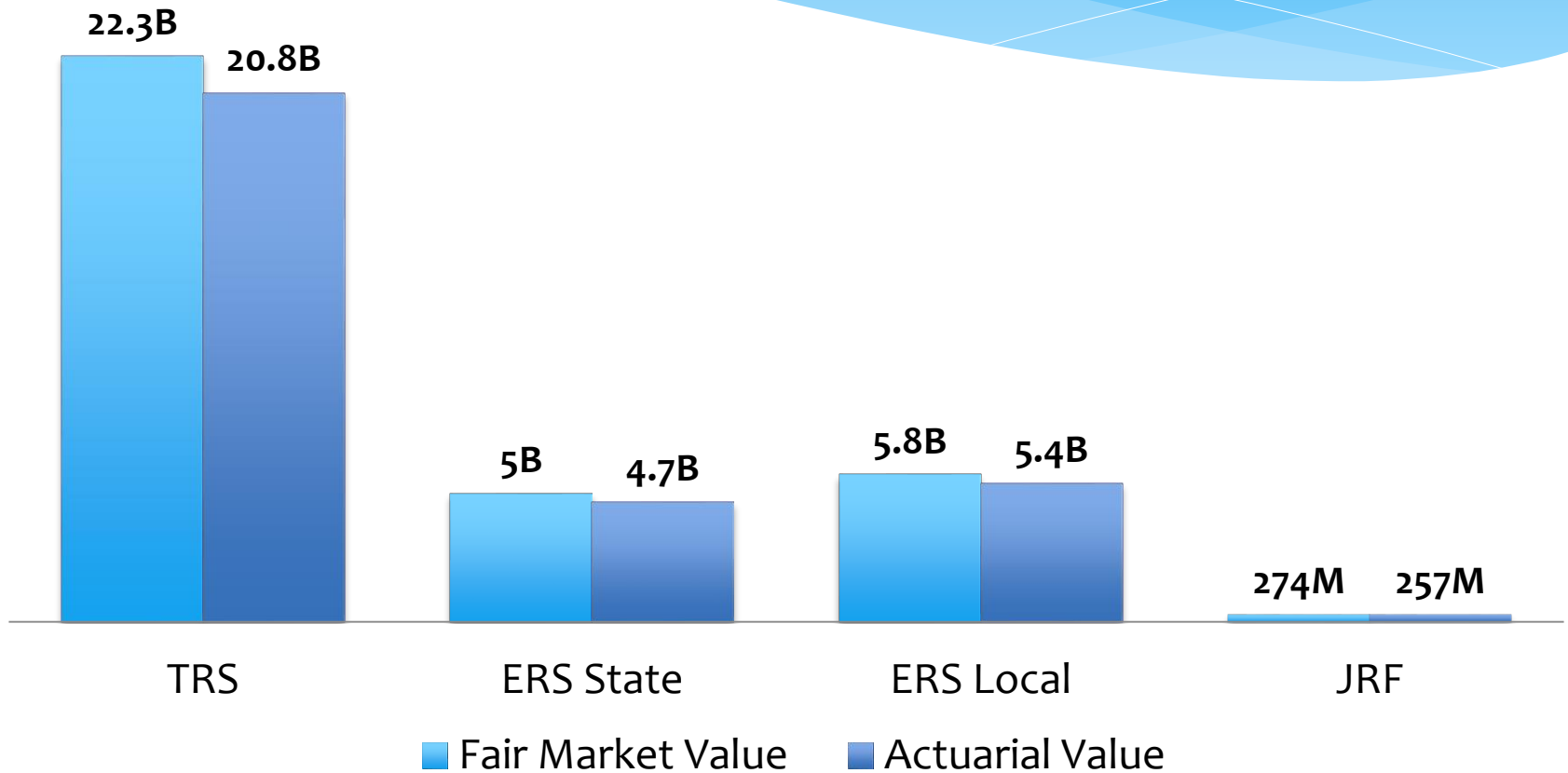
# Who Are RSA's Members?

| (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?

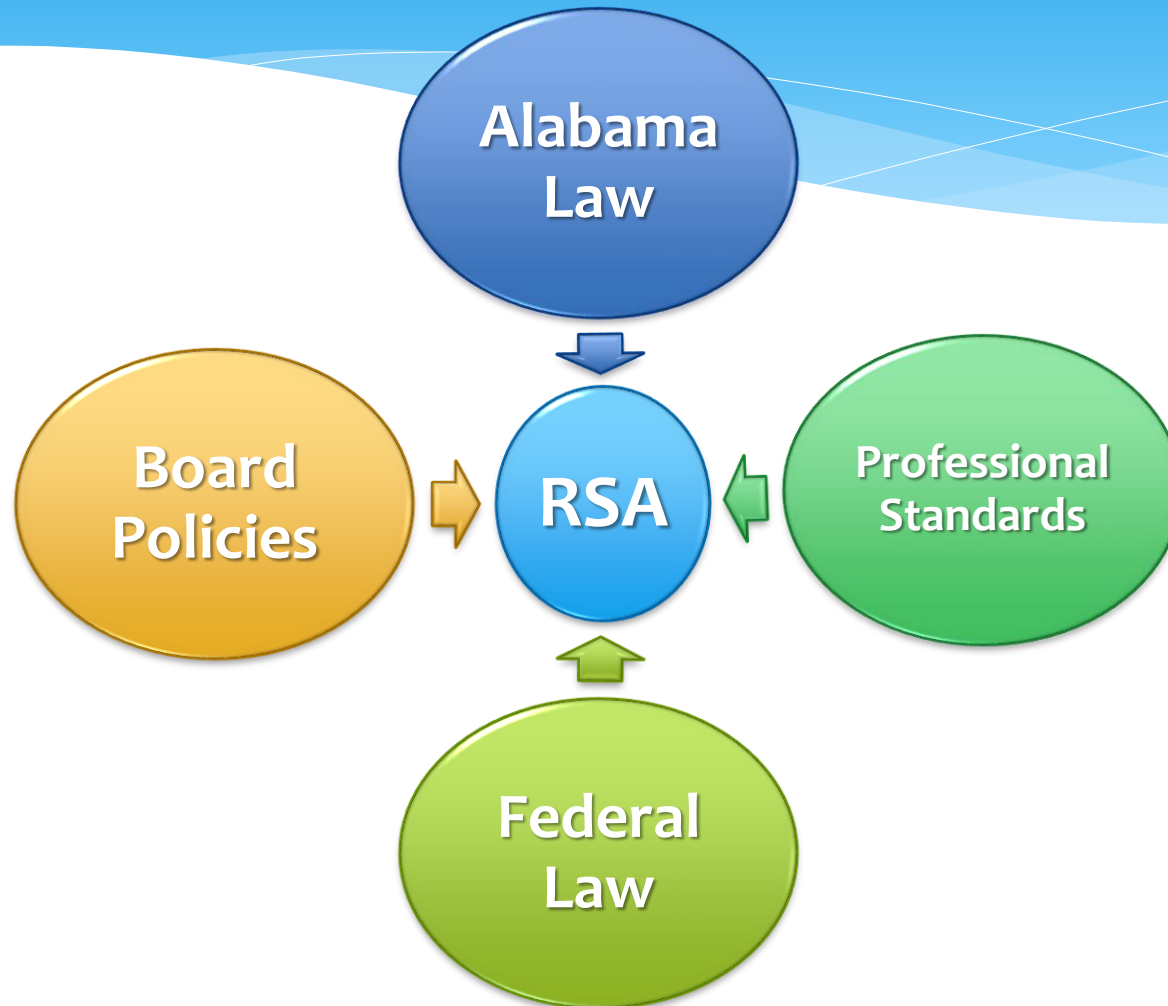


# Funding Levels as of 9/30/14





# 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 industry 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

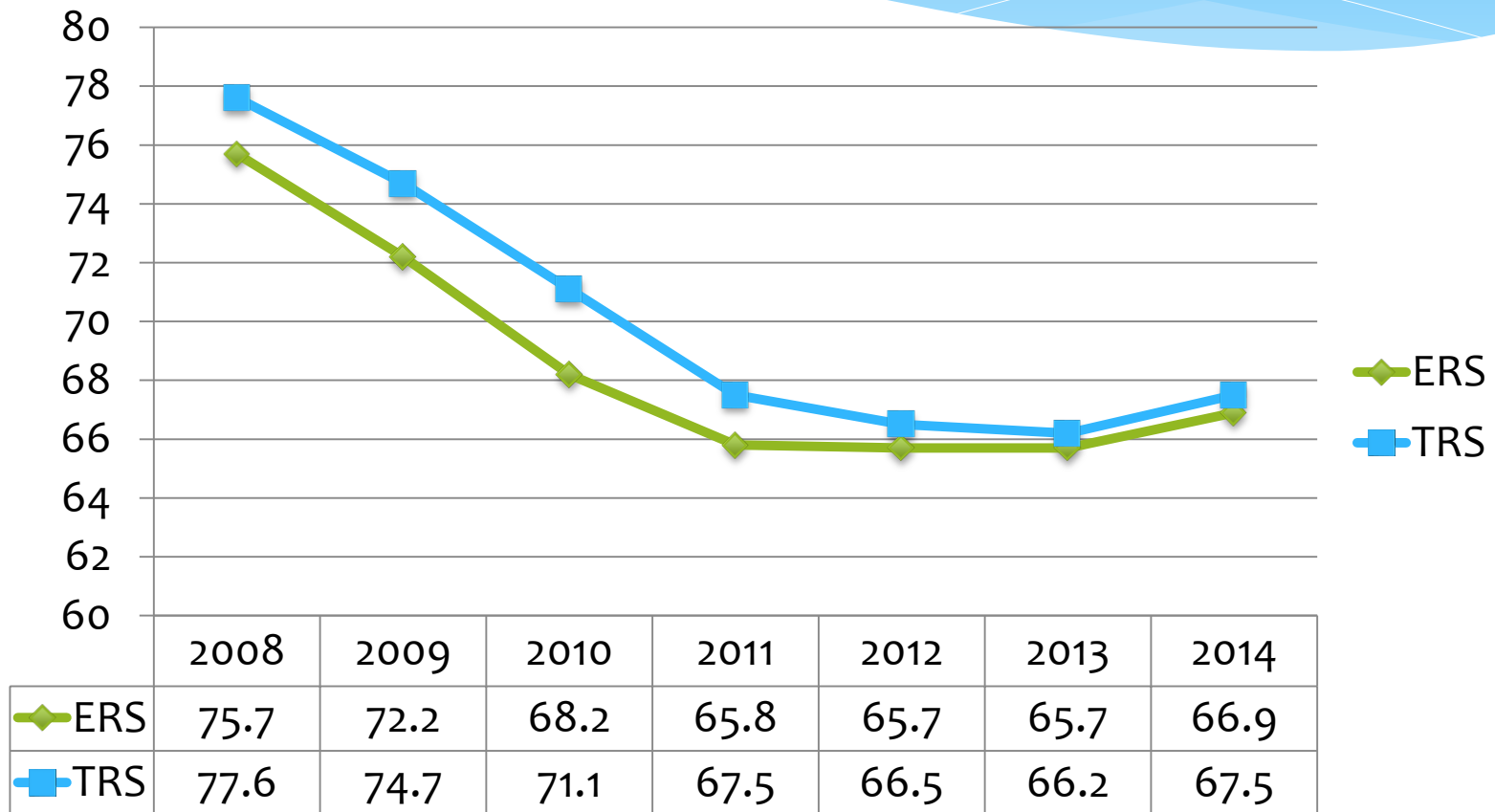
## Public Records Act

- ◆ 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.**