

Employees' Retirement Board Of Rhode Island Monthly Meeting Minutes Date of Meeting: September 8, 2004

The Monthly Meeting of the Retirement Board was called to order at 9:05 a.m., Wednesday, September 8, 2004, in the 8th Floor Conference Room, 40 Fountain Street, Providence, RI.

I. Roll Call of Members

The following members were present at roll call: Ponzi A. Angelone; Daniel L. Beardsley; Michael R. Boyce; Liza Cohen, designee for Representative Steven M. Costantino; William B. Finelli; John P. Maguire; General Treasurer Paul J. Tavares and Jerome F. Williams, designee for the Director of Administration.

Also in attendance: Frank J. Karpinski, ERSRI Executive Director and David D. Barricelli, Board Counsel.

Recognizing a quorum, Treasurer Tavares called the meeting to order.

Rosemary Booth-Gallogly arrived at 9:05 a.m.

Roger Boccanfuso arrived at 9:10 a.m.

Linda C. Riendeau arrived at 9:20 .m.

II. Approval of Minutes

On a motion by Jerome F. Williams and seconded by Michael R. Boyce, it was

VOTED: To approve the minutes of the August 11, 2004 meeting of the Employees' Retirement System of Rhode Island Board.

III. Chairman's Report

Treasurer Tavares told the Board that at the last meeting Mr. Beardsley asked for a brief summary of the work done by the Pension Review Team. He asked Mr. Williams, who is a member of the Team, to provide the review.

Mr. Williams reported that the Team began in October 2003. He pointed out that there were five (5) phases of the review. First, there was a comparative analysis of public plans. Second, there was a data analysis based on information gathered from the current plan, the demographics of the plan, and funded status. Third, there was an analysis by Gabriel, Roeder, Smith and Company (GRS) that looked at future trends and projections. In the fourth phase, the commission did some actuarial modeling on the proposed changes. Mr. Williams pointed out that there were no items excluded from the analysis. Lastly, the commission developed recommendations to review.

Mr. Williams then summarized some of the findings. He told the Board that in a comparative analysis of public pension plans, Rhode Island maintains a lower requirement on years-to-retain than most plans, has a longer vesting period than most plans (Rhode Island's is 10 years and many plans require only 5 years) and employee contribution rates in Rhode Island are among the highest nationwide (State employees contribute at a rate of 8.75% and Teachers at 9.50%).

He further told the Board that based on the analysis, fifty percent (50%) of the top 100 public pension plans have guaranteed COLAs at a fixed percentage or COLAs tied to CPI. Of the 100 plans, 32 had COLAs tied to the CPI. He said the analysis also indicated that in 35% of the plans studied, pension benefits were not subject to taxation. Mr. Williams told the Board that the study also indicated that 76 % of the plans had funded ratios greater than 80% and many of the others were at 100% or over. At the time the study was performed, Rhode Island was at a funding level of 63.1% for Teachers and 61.5% for State employees. Mr. Williams added, based on the analysis by GRS, Rhode Island's funding ratio was projected to decline over the next 3 years.

Based on some of the projections, Mr. Williams pointed out the variance between fiscal year employer contribution rates. He said for fiscal year 2003 the contribution rate was 9.6%, and in fiscal year 2007 the rate will go to 18.2% if no action is taken to address the current situation. He added that the dollar value of contributions by the state of Rhode Island for fiscal year 2003 was \$58 million, and in 2007 the amount would increase to \$124 million. He pointed out that these numbers reflect a 113% increase in 5 years. Mr. Williams then told the Board that the employer contribution rate for teachers was 13.72% in fiscal year 2003 and would increase to 22.5% in fiscal year 2007. In dollar amounts, contributions would increase from \$112 million in fiscal year 2003 to \$207 million in fiscal year 2007. Mr. Williams apprised the Board that the numbers mentioned did not include the changes in assumptions that were presented to the Board in July.

Mr. Williams concluded his presentation and pointed out to the Board that the first and foremost reason for the review team was to insure the long term financial integrity of the system and to have an equitable pension plan for employees. He said these two goals were carried out through the entire review process.

Mr. Williams provided the Board with a summary of proposals from the Department of Administration. The first proposal would be that when the State has a surplus of over \$30 million dollars, 50% of that surplus would be allocated directly to the pension system and to the retiree health plan because those liabilities are the largest unfunded liabilities that are facing the State.

Second, he proposed that for new hires and employees with 10 years of service and less, there would be a change in the benefit schedule. Eligibility for benefits would be at a minimum age of 57 and 28 years of service or a minimum age of 65 with 10 years of service.

Finally, he proposed a change in the accrual formula that would modify percentages on an annual basis and would provide unreduced benefits at 80% at 38 years rather than the current 35 years. He also proposed a COLA based on the CPI with a 3% cap. Mr. Williams pointed out that based on the study performed the COLA modification would reduce employer contributions for State Employees by \$11 million and \$23 million dollars for State Employees and Teachers respectively.

Mr. Williams told the board that members of the Pension Review Team representing labor presented recommendations that were primarily funding proposals. He said they proposed that any revenues from the sale of surplus property, excess gambling revenues above FY2005 amounts, sinking fund or refunding bond savings, be deposited into the pension fund. The Labor members also proposed legislation mandating full funding of the pension system. Mr. Williams pointed out that Treasurer Tavares also proposed a pension review every 5 years.

Treasurer Tavares, who is also a member of the Pension Review Team, apprised the Board of proposals prepared by his office. He told the Board that one of the goals of the review, and a primary objective, was to have data that everyone trusted. He told the Board that large unfunded pension liabilities are not contained to Rhode Island but it is a global issue. In fact, he referenced a study which indicated 50 of the largest European private defined benefit plans presently have an unfunded liability in excess of \$139 billion. He told the Board that both his proposal and Mr. Williams' proposals are an attempt to mitigate the effects of increased unfunded liabilities. He pointed out to the Board that his proposal was remedial at best and there should be ongoing efforts to remedy the system and constantly monitor long-term effects.

Treasurer Tavares provided the Board one example of an item that should be addressed for long-term consideration namely, the social security retirement option currently offered. He thought it would be prudent to determine if this option entices members to retire earlier and to also prepare an analysis of the actual cost to the system. He felt it would also be prudent to analyze the taxability issues of pensions since Rhode Island appears to be one of the few systems to tax pensions.

Treasurer Tavares noted that one of the challenges facing the Retirement System is that Rhode Island does not have a minimum retirement age. He proposed instituting a minimum retirement age of 55 years and pointed out that Mr. Williams proposed age 57 as a minimum retirement age.

He also proposed modifying the current benefit formula to 75% of final average salary after 38 years of service. He proposed maintaining the current formula of a service allowance for those members with 10 years of service and age 60. The Treasurer noted the difference between the two proposals as Mr. Williams' proposed formula was 10 years of service at age 65.

Treasurer Tavares proposed a cap of 3% for COLAs which would be tied to the consumer price index (CPI). He also emphasized that all of his proposed changes would affect new and non vested members. In order to mitigate some costs, the Treasurer proposed that the COLA modification would affect all active employees not currently eligible to retire. Regarding funding, Treasurer Tavares suggested that 30% of the savings derived from the proposed benefit modifications be put back into the system to reduce the unfunded liability. Over a 20 year period, he estimates the savings would amount to over \$700 million dollars that would revert back into the fund. Treasurer Tavares suggested that other sources of income be looked into such as the revenues from the refunding bond authority and the sinking fund. He said that either by statute or constitutional amendment there should be provisions for mandating full funding of the pension system as deemed by the actuary and that there be an ongoing review to monitor developments in the system. Treasurer Tavares agreed that the proposed measures are severe but only remedial. He affirmed that he did not want to mislead anyone that either his or Mr. Williams' proposals resolve the long-term problems facing the Retirement System.

Mr. Beardsley thanked Treasurer Tavares and Mr. Williams for their presentations and extended an offer to members of organized labor to appear in front of the Board to provide details of their proposals. He told the Board that although he understood the Board's role in formulating public policy, he felt it was incumbent upon the Board to impress upon the General Assembly the absolute necessity for fiscal discipline for full funding of the system.

Both Treasurer Tavares and Mr. Williams emphasized Mr. Beardsley's concern for fiscal discipline by its relation to rating agencies. They both felt the State's bond rating would suffer from low funding ratios.

Mr. Maguire then referred to a newspaper article that reported the pension commission was somewhat surprised by the numbers that were reported to the Board by GRS. He asked Director Karpinski as to when GRS had an indication of the magnitude of the numbers and if that information was known prior to the pension commission finishing its study. Director Karpinski responded stating that GRS had raw information about 2 to 3 weeks before the July Board meeting, primarily demographic type information. He further stated that the finalized numbers were not available until less than a week before the meeting. Director Karpinski pointed out a few issues. First, GRS was in the midst of a conversion to new software from its prior parent corporation Watson Wyatt Worldwide to Gabriel, Roeder, Smith and Company; this may have added some time to completion of the study. Second, due to recent law suits against other large actuarial firms and limited liability disputes, actuarial firms in general are less willing to release estimated information prior to completion of formal internal reviews by their organizations; this may also have contributed to the timing of having final numbers. Lastly, Director Karpinski told the Board that some information from ERSRI was provided late to GRS.

Treasurer Tavares indicated to Mr. Maguire that he had been accused of manipulating the timing of the study and perhaps the content. Treasurer Tavares told the Board this was completely inaccurate and he assured the entire Board that he had no involvement in the process. He further stated that the timing of the study was consistent with what has been done in prior years.

IV. Executive Director's Report

Director Karpinski addressed the request from the last Board meeting regarding an actuarial audit. He pointed out that he had done research with other system directors and actuarial firms. The most common practice was to have the auditing actuary replicate the most recent plan valuation. This is done to ensure the reasonableness and appropriateness of the valuation methods, assumptions, certifications and conclusions of the consulting actuary. It also provides a determination of whether the consulting actuary's valuation procedures are technically sound and based on generally accepted actuarial standards. The replication also ensures that the valuation results, including a review of the data used and mathematical calculations are accurate. Director Karpinski then told the Board the next item of review should be the experience study. He recommended that the Board consider having the auditing actuary comment on the results prepared by GRS or if they felt compelled, to have the auditing actuary replicate the experience study and provide comments.

Director Karpinski told the Board that the process of selecting an auditing actuary would be similar to the process employed when GRS was hired. Treasurer Tavares

suggested that an RFP be prepared to ask proposing firms to provide fees on all of the individual scenarios described by Director Karpinski. He said the Board could then select the options based on their questions of the candidates.

Treasurer Tavares then asked that Director Karpinski prepare a draft RFP and assemble the procurement subcommittee to begin the approval process of the RFP. Director Karpinski informed the Board that the timing of the audit was in line with other public pension systems. He stated that “best practices” by other systems and the GFOA recommend an audit every 7-10 years. He reminded the Board that GRS did a replication audit 7 years ago when it was hired to replace William M. Mercer Co., Inc., thus he reiterated the timing was perfect to do another audit.

Director Karpinski presented the Pension Application Report. He pointed out that there were a substantial number of retirees processed and commended the staff for a job well done.

V. Administrative Decisions

Disability Appeals:

(None this month)

Hearing Officer Decisions:

Nancy White vs. ERSRI

Attorney Barricelli advised the Board that he confirmed with Nancy White’s representative that she has decided not to pursue her appeal. Attorney Barricelli recommended that the hearing officer’s decision be affirmed.

On a motion by Ponzi A. Angelone and seconded by Michael R. Boyce, it was unanimously

VOTED: To affirm the decision of the hearing officer.

VI. Approval of August pensions as presented by ERSRI

On a motion by Michael R. Boyce and seconded by Rosemary Booth-Gallogly, it was unanimously

VOTED: To approve the August pensions as presented by ERSRI.

VII. Legal Counsel Report

Attorney Barricelli directed the Board to the legal report in the book and asked if there were any questions. In addition, he apprised the Board of the Merolla vs. City of Providence matter in which the Board is involved as an interested party. He referred the Board to the decision that was mailed to them by Director Karpinski.

The Merolla decision has to do with the interpretation of Rhode Island General Law §16-16-24 and its effect on the post retirement employment of a former coach in the City of Providence. The court decision reinstates Mr. Merolla to his position as Coach of the Mt. Pleasant High School football team and orders the City of Providence to reimburse him approximately \$10,000 in salary. Attorney Barricelli informed the Board that he felt that this decision is flawed, and recommended that the Board appeal this decision.

Attorney Barricelli pointed out that there are several other coaches, such as Mr. Badway, who was discussed at the prior month's board meeting, who will be affected by this ruling. He told the Board that there could be legal issues that spill over to the Providence Coaches case that is currently in Superior Court pending. He further apprised the Board that in the Providence Coaches matter the plaintiffs are currently seeking a declaratory judgment on the issue of whether or not coaching salaries should be included in the computation of their salary for retirement purposes and if so contributions should be made to the retirement system on coaching salaries.

Attorney Barricelli explained to the Board that the Merolla vs. City of Providence matter was technically a cross motion for summary judgment. He said the standard for summary judgment is that the judge looks at the facts in the light most favorable to the party that is opposing the summary judgment. Attorney Barricelli then said that if the system opposes the summary judgment and if it comes down to interpretations and decisions, the court is required, under this standard, to give the benefit of the doubt to the opposing party. Thus, he said ERSRI should have been given the benefit of a doubt in this matter.

Attorney Barricelli said the judge made a determination that Mr. Merolla's status had not changed. Attorney Barricelli felt that Mr. Merolla's status had changed; he went from a vested contributing participant to an inactive retired individual in the system; within the Retirement System he went from not collecting a pension to collecting a pension and from contributing to non-contributing. Attorney Barricelli felt that the judge erred on this issue. Attorney Barricelli then summarized some of the language in the decision where he found other error's in law.

Mr. Beardsley then made a motion to file an appeal, it was opened for discussion. Mr. Maguire and Mr. Finelli both stated that they would oppose the motion.

Treasurer Tavares indicated that he challenged it because he felt it was more of a policy issue and has nothing to do with retirement. The issue is who can be a coach and who the position has to be offered to. Treasurer Tavares was concerned about pension fund money being spent to defend a position that should be dealt with at the General Assembly.

Treasurer Tavares then asked for a roll call vote to file an appeal in this matter. The following members voted in favor of the motion: Ponzi A. Angelone, C.L.U., Daniel L. Beardsley, Liza Cohen, Rosemary Booth-Gallogly, Treasurer Paul J. Tavares and Jerome F. Williams. The following members voted nay: Roger Boccanfuso, Michael R. Boyce, William B. Finelli, John P. Maguire and Linda C. Riendeau. There being only 6 votes in the affirmative, the motion failed.

Since the motion failed, Treasurer Tavares asked Attorney Barricelli to provide instruction to the Board on how to proceed in complying with the Merolla vs. City of Providence decision. Attorney Barricelli informed the Board that based on the decision, he recommended that the matter involving Mr. Badway be adjudicated consistent with the Merolla decision since the facts are similar.

(Prior to the commencement of the Badway matter Mr. Maguire recused himself from any and all consideration on the matter)

On a motion by Daniel L. Beardsley and seconded by Michael R. Boyce, it was unanimously

VOTED: To reverse the Decision of the Hearing Officer and to approve the appeal of Jon Badway vs. ERSRI.

At the conclusion of the vote, Treasurer Tavares advised all board members to contact the General Assembly to clarify the intent and language of the above case.

Attorney Barricelli apprised the Board of the telephone response received from the IRS regarding the Private Ruling Letter ruling that was submitted regarding § 415(b). He said the IRS answered in the affirmative regarding the systems question stating that the maximum benefit payable under section 415 must be reduced to reflect the value of the cost of living adjustment provided under section §36-10-35 as of the members retirement date, even though the adjustment does not begin until January 1st following the 3rd anniversary of the members retirement date.

Attorney Barricelli told the Board that the IRS provided another opinion regarding the question of existing retirees and whether or not their benefits would need to be reduced and any excess benefits be recouped. He said the IRS stated that ERSRI must recoup and reduce existing benefits. Attorney Barricelli then summarized for the Board the new procedure from the IRS regarding self-correction. He pointed out that the IRS provided him the specific sections of the code that dealt with such matters and he was currently analyzing them. He pointed out that by using this procedure there would be no fine or penalty levied against ERSRI.

Treasurer Tavares asked Director Karpinski to analyze the potential affected members so the Board could determine the best method of compliance with the IRS ruling. Director Karpinski said he will compile the data and report back the findings.

On a motion by Ponzi A. Angelone and seconded by Jerome F. Williams, it was unanimously

VOTED: To have Attorney Barricelli inform the IRS that the Board would not request a conference and for them to issue a private letter ruling.

Ms. Booth-Gallogly asked Director Karpinski if it would be possible to modify the web site to do estimates using the new 415(b) amounts. Director Karpinski told Ms. Booth-Gallogly that the website already does 415(b) computations using the 2002 415(b) amounts; he said he would begin the process of including the new amounts inclusive of COLA. Treasurer Tavares also requested that potential affected retired members be notified by letter.

Finally, Attorney Barricelli apprised the Board that the Cranston Crossing Guards case has been scheduled for a hearing for September 30, 2004.

VIII. Committee Reports

Disability Sub-Committee: The Disability Sub-Committee recommended the following actions on disability applications as the result of its September 3, 2004 meeting for approval by the full Board:

	Name	Membership Group	Type	Action
1.	Clare Burns	Teacher	Ordinary	Approve
2.	Marina Carnevale	State	Ordinary	Approve
3.	William French	Municipal	Ordinary	Approve
4.	Clement Labine	State	Ordinary	Approve
5.	Paula Pedulla	Municipal	Ordinary	Approve
6.	Brian Martin	Municipal	Accidental	Approve
7.	Michael Warner	State	Accidental	Approve

On a motion by William B. Finelli and seconded by Michael R. Boyce it was unanimously

VOTED: To approve the recommendation of the Disability Sub-Committee meeting on Friday, September 3, 2004 on items 2, 3,4,5,6.

On a motion by William B. Finelli and seconded by Michael R. Boyce it was unanimously

VOTED: To approve the recommendation of the Disability Sub-Committee meeting on Friday, September 3, 2004 on item 1.

(Mr. Maguire recused himself from any and all consideration of item 1).

On a motion by William B. Finelli and seconded by Michael R. Boyce it was unanimously

VOTED: To approve the recommendation of the Disability Sub-Committee meeting on Friday, September 3, 2004 on item 7.

(Mr. Boccanfuso recused himself from any and all consideration of item 7).

IX. New Business

Treasurer Tavares raised outstanding issues from the experience study regarding salary increase rates for State Employees and asked Director Karpinski to address the issue for the Board. Director Karpinski briefly discussed a memorandum that was included in the Board's book describing the results of the review done by GRS, ERSRI and the Department of Administration on the salary increase rate assumption. He pointed out that GRS revised its analysis and recommended a revision to the proposed new salary increase rates for State Employees presented at the July Board meeting. Based on the new recommended salary increase rates, the new contribution rate would be a 23 basis point decrease to 16.96%

Given the information presented on a motion by Rosemary Booth-Gallogly and seconded by Jerome F. Williams, it was unanimously

VOTED: To approve the assumptions for the State Employees Plan as recommended by the actuary with the new salary assumption rate as described in the memorandum.

On a motion by Rosemary Booth-Gallogly and seconded by Jerome F. Williams, it was unanimously

VOTED: To retain the assumed rate of investment rate return at 8.25% for State Employees.

Director Karpinski then informed the Board that now that all assumptions were acted on, the actuary would be at the October Board meeting to present the FY 03 valuation results for all plans.

X. Adjournment

There being no other business to come before the Board, on a motion by William B. Finelli and seconded by Michael R. Boyce, the meeting was adjourned at 10:35 a.m.

Respectfully submitted,

Frank Karpinski

Executive Director