

MINUTES of Regular SERS Board Meeting - Wednesday, March 9, 2016

CALLED TO ORDER: 9:30 a.m. by Chairman David R. Fillman

ATTENDEES:

Members and Designees

David R. Fillman – Chairman

Stephen S. Aichele

Glenn E. Becker

Dan B. Frankel

Robert W. Godshall

Vincent J. Hughes

Charles T. McIlhinney, Jr.

Michael V. Puppio, Jr.

M. Joseph Rocks

Christopher Craig – Designee for Treasurer Timothy A. Reese

Charles Duncan – Designee for Senator Vincent J. Hughes

Bernie Gallagher – Designee for Representative Dan B. Frankel

Dan Ocko - Designee for Representative Dan B. Frankel

Ned Smith - Designee for Representative Robert W. Godshall

Consultants

Ian Bray, RVK, Inc.

Perry Christie, Empower Retirement

Shelby Dobson, Empower Retirement

Rob Kochis, The Townsend Group

Brent Mowery, Hay Group, Inc.

Matt Roche, StepStone Group LLC

Jim Rohlinger, Empower Retirement

Jim Voytko, RVK, Inc.

Executive Staff

Thomas F. Brier

David E. Durbin

Anthony Faiola

N. Joseph Marcucci

Staff

Rose Agnew

Eric Baker

Karen Damiano-Stahler

Dino Degennaro

Patricia Dence

Linda Engle

David Felix

Pamela Hile
Meredith Jones
Barbara Kiral
Cheryl Krchnar
Karen Lynn
Sara McSurdy
Jeffrey Meyer
James Nolan
Jay Pagni
Steven Rosenberry
David Sedlak
Sharon Smith
David Tarsi
Joseph Torta
William Truong

Visitors

Chris Ade, Lord, Abbett & Co., LLC
Amy C. Brown, Goldman Sachs Asset Management
Brook Critchfield, HarbourVest Horizon
Peter Cunningham, BNY Mellon
Jim Kane, Unite Here
Todd Kowalski, Public Financial Management
Sandy Leopold, PA Department of Treasury
Dave Starr, Public Financial Management
Kevin Sullivan, BNY Mellon

Presenters

None

MINUTES of the Regular SERS Board Meeting Wednesday, March 9, 2016

A. ANNOUNCEMENT OF PERSONNEL SEARCH COMMITTEE

Chairman Fillman acknowledged that SERS Chief Investment Officer, Mr. Thomas Brier, has submitted his letter of retirement to be effective June 24, 2016. The board has designated Senator McIlhinney to lead the search for a new CIO.

B. Investment Presentations and Reviews: SERS INVESTMENT OFFICE AND RVK, INC.

Presentation: 1. Capital Market Report

Messrs. Voytko and Bray presented the report provided to the board (3/9/2016 board handouts).

Presentation: 2. SERS Quarterly Performance Report (as of December 31, 2015)

Messrs. Voytko and Bray presented the report provided to the board (3/9/2016 Board Package, Investment Report, Tab 6 and board handouts).

Presentation: 3. Investment Manager Fee Review Discussion

Messrs. Voytko and Bray presented the report provided to the board (3/9/2016 Board Package, Investment Report, Tab 5).

C. Investment Presentations and Reviews: SERS INVESTMENT OFFICE AND RVK, INC.

Presentation: 1. Global Equity – Emerging Manager Program Framework Discussion

Messrs. Voytko and Bray presented the report provided to the board (3/9/2016 Board Package, Investment Report, Tab 7).

D. THE HAY GROUP AND RVK, INC.

Action: 1. 2015 Actuarial Valuation – Investment Return Assumption Discussion

Messrs. Mowery and Voytko presented the report provided to the board (3/9/2016 Board Package, Administrative Report, Tab 12 and board handouts.)

MOTION: 2016-11

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board adopts, effective with the December 31, 2015 valuation, the actuarial assumptions set forth in the Hay Group's 2011-2015 Actuarial Experience Study and the recommended changes to the current actuarial valuation assumptions, based upon Hay Group's 2011-2015 Actuarial Experience Study, as set forth in the attached "Summary of Recommended Changes to Actuarial Valuation Assumptions Based Upon 18th Investigation of Actuarial Experience Covering the Period January 1, 2011 to December 31, 2015 To Be Effective With the December 31, 2015 Actuarial Valuation" (ATTACHMENT A).

MOTION: 2016-12

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board accepts the recommendation of Hay Group to leave

unchanged the current annual assumed rate of investment return and assumed rate of inflation and to adopt an annual assumed rate of investment return of 7.5% compounded annually and an annual assumed rate of inflation of 2.75% compounded annually, with both assumptions to be effective with the December 31, 2015 Actuarial Valuation and to remain in effect until changed by the board.

E. EMPOWER RETIREMENT, THIRD PARTY ADMINISTRATOR

Presentation: 1. DCP Presentation

Mses. Engle and Dobson and Messrs. Faiola, Christie and Rohlinger presented the report provided to the board (3/9/2016 Board Package, Administrative Report, Tab 11).

F. STANDARD MOTIONS

Action: 1. Minutes of Board Meeting – January 27, 2016

Chairman Fillman presented the report provided to the board (3/9/2016 Board Package, Administrative Report, Tab 2).

MOTION: 2016-13

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board approves the minutes of the January 27, 2016 board meeting.

Action: 2. Statement of Changes in Fiduciary Net Position for Period Ending – December 31, 2015

Chairman Fillman presented the report provided to the board (3/9/2016 Board Package, Administrative Report, Tab 3).

MOTION: 2016-14

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board accepts the State Employees' Retirement System's Statement of Changes in Fiduciary Net Position for the period ending December 31, 2015.

G. EXECUTIVE SESSION

Presentation: 1. Agenda

At 12:00 p.m., the board recessed and entered executive session to receive legal advice and confidential performance information on executive session agenda items, as attached (ATTACHMENT B).

H. LUNCH BREAK

I. PUBLIC MEETING RESUMES

The public meeting resumed at 1:18 p.m.

J. REPORT FROM CHIEF INVESTMENT OFFICER

Action: 1. Consultant Contracts – RVK, Inc. and StepStone Group LLC

Chairman Fillman noted that the following motions were a result of discussion in executive session.

MOTION: 2016-15

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board authorizes staff to amend the agreement between PA SERS and RVK, Inc. to facilitate a 24-month extension of the current General Consulting Agreement and its corresponding amendments under the existing terms, services, and fee schedules, subject to successful completion of contract negotiations and execution and delivery of closing documents by all parties, including required Commonwealth legal approvals, within six months.

MOTION: 2016-16

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board authorizes staff to amend the agreement between PA SERS and StepStone Group LLC to facilitate a 12-month extension of the current Alternative Investment Consulting Agreement and its corresponding amendments under the existing terms, services, and fee schedules, subject to successful completion of contract negotiations and execution and delivery of closing documents by all parties, including required Commonwealth legal approvals, within six months.

MOTION: 2016-17

By motion that was moved, seconded, and approved by board members, it was

RESOLVED: That the board terminates the Wellington Diversified Inflation Hedges Portfolio managed by the Wellington Trust Company NA, and reallocates 100 percent of the assets to the MCM MSCI World Ex US Index.

K. REPORT FROM EXECUTIVE DIRECTOR

Presentation: 1. Board Dismissal

Mr. Durbin noted that the report was provided to the board (3/9/2016 Board Package, Administrative Report, Tab 7).

Presentation: 2. Audit Committee Member Reappointment

Mr. Durbin noted that board member, Stephen S. Aichele, has agreed to continue serving on the Audit Committee. His term will expire 12/31/2018.

Presentation: 3. Deferred Compensation Committee Meeting Minutes – January 27, 2016

Mr. Durbin noted that the report was provided to the board (3/9/2016 Board Package, Administrative Report, Tab 9).

Presentation: 4. Legislative Update

Mr. Durbin noted that the report was provided to the board (3/9/2016 Board Package, Administrative Report, Tab 8). SERS appeared before the House Appropriations Committee on Monday, March 7, 2016.

Presentation: 5. 2015 Member Statement

Mr. Durbin noted that a sample of the 2015 Member Statement has been placed at each board member's seat (3/9/2016 board handouts).

L. NEXT BOARD MEETING – APRIL 27, 2016

Chairman Fillman noted that the next regular meeting of the SERS board is scheduled for April 27, 2016 with a start time of 10:30 a.m.

M. MOTION TO ADJOURN

Action: 1. Adjournment

MOTION: 2016-18

By motion of Chairman Fillman, the board unanimously agreed to adjourn the meeting at 1:23 p.m.

Respectfully submitted,



David E. Durbin
Executive Director

Summary of Recommended Changes to Actuarial Valuation Assumptions Based Upon 18th Investigation of Actuarial Experience, Covering the Period January 1, 2011 to December 31, 2015, To Be Effective With the December 31, 2015 Actuarial Valuation

I. Economic Assumptions

Career Salary Increase Assumptions: Since actual career salary increases observed over the study period were lower than expected, with significantly lower rates of salary growth in the first few years of employees' careers, Hay Group recommends reductions at every service level, ranging from 0.15 percent to 2.0 percent decreases, and averaging about 0.4 percent lower. The table below shows the specific assumptions being recommended:

Years of Credited Service	Current Assumed Annual Increase in Career Salary	Recommended Assumption - Annual Increase in Career Salary	Years of Credited Service	Current Assumed Annual Increase in Career Salary	Recommended Assumption - Annual Increase in Career Salary
1	8.00%	6.00%	16	2.50%	2.10%
2	6.00%	4.50%	17	2.40%	2.05%
3	4.50%	4.00%	18	2.30%	2.00%
4	4.00%	3.75%	19	2.20%	1.95%
5	3.75%	3.50%	20	2.10%	1.90%
6	3.50%	3.25%	21	2.00%	1.85%
7	3.25%	3.00%	22	1.90%	1.75%
8	3.20%	2.90%	23	1.80%	1.65%
9	3.15%	2.80%	24	1.70%	1.55%
10	3.10%	2.70%	25	1.60%	1.45%
11	3.00%	2.60%	26	1.50%	1.25%
12	2.90%	2.50%	27	1.40%	1.05%
13	2.80%	2.40%	28	1.30%	0.90%
14	2.70%	2.30%	29	1.25%	0.85%
15	2.60%	2.20%	30+	1.25%	0.80%

II. Demographic Assumptions

- a. Annuitant Mortality Assumptions: Although the actual 2011-2015 mortality experience of SERS annuitants did not deviate significantly from our current assumed death rates, the current rates are under-predicting total deaths for non-disabled annuitants and over-predicting total deaths for disabled annuitants. In

order to provide margin for future mortality improvement, we recommend these assumptions be adjusted so they predict relatively fewer deaths (by 5% - 10%) than the number that have actually been occurring in the latest experience. Therefore, we recommend the following updated mortality assumptions:

Male Non-Disabled: RP-2000 Male Combined Healthy (CH) Mortality Table projected 16 years (to 2016) using Scale AA, with lower rates at ages 83-92 (to provide 10% margin for improvement)

Female Non-Disabled: RP-2000 Female CH Mortality Table projected 20 years (to 2020) using Scale AA, with lower rates at ages 64-80 (to provide 10% margin for improvement)

Male Disabled: RP-2000 Male Disabled Retiree Mortality Table projected 21 years (to 2021) using Scale AA (to provide 6% margin for mortality improvement)

Female Disabled: RP-2000 Female Disabled Retiree Mortality Table projected 17 years (to 2017) using Scale AA (to provide a 5% margin for mortality improvement)

- b. Superannuation Retirement Assumptions Applicable to General Employees (i.e., Classes AA and A): In general, for both males and females, (i) relatively fewer employees are retiring at, or prior to, the earliest superannuation age and (ii) relatively more are deferring retirement until Social Security Retirement Ages (65-66) or beyond. Therefore, we recommend:

For Males: Lower retirement rates prior to age 59 and

For Both Males and Females: Higher retirement rates after age 65

- c. Other Demographic Assumptions:

i. **Applicable to all active employees, we recommend -**

1. Slight increases to male mortality rates; no changes to female mortality rates
2. Increases to disability retirement rates for both males and females
3. Increases to employee withdrawal rates for both males and females

ii. **Applicable to general (Classes AA and A) employees, we recommend -**

1. Increases to early retirement rates for those with 15+ yrs of service for both males and females
2. Significant increases to early retirement rates for those with < 15 yrs of service for both males and females

iii. **Applicable to employees in various special benefit classes, we recommend -**

1. Changes to superannuation rates as follows: Increases for state police (> 19 yrs service) and other hazardous duty employees; decreases for legislators and judges/justices
2. Changes to early retirement rates as follows: Increases for state police, other hazardous duty employees and judges/justices; decreases for legislators
3. Changes to withdrawal rates as follows: Decreases for state police, other hazardous duty employees, judges/justices and legislators

III. Special Assumptions

- a. Form of Payment: This experience study included a review of the forms of payment elected by retiring SERS participants over the 2011-2015 period. Based upon this experience, we recommend minor adjustment to the current Form of Payment assumptions as follows:

<u>Form of Payment</u>	<u>Current Assumptions</u>	<u>2011-2015 Experience</u>	<u>Recommended Assumptions</u>
I. Single Life Annuity	33%	32.0%	32%
II. Option 1 (Guaranteed PV) OR Option 1 combined with joint and survivor Option	41%	42.7%	43%
III. Option 2 (100%) or 3 (50%) or other % to survivor	26%	25.3%	25%
IV. Total	100%	100.0	100%

- b. Probability of Electing Full Option 4 Withdrawal: This experience study included a review of the contributions and interest actually withdrawn by retirees out of the total contributions and interest available for withdrawal over the 2011-2015 period. Based upon our findings, we recommend that the current percentage of retirees assumed to elect a full Option 4 withdrawal of contributions and interest be revised as follows:

<u>From Current Assumption of:</u>	<u>To Recommended Assumption of:</u>
85%	80%

ATTACHMENT B

EXECUTIVE SESSION AGENDA Meeting: March 9, 2016

Executive Session

1. Notational Ballot

**Account of Lynn D. Wilson (Deceased)
Docket No. 2014-04
Claim of Donna Killinger**

2. Pending Litigation Update

3. Fund Update

4. Preliminary Fund Performance and Risk Statistics

5. Manager Update