PUBLIC OVERSIGHT HEARING ON THE OTHER POST-EMPLOYMENT BENEFITS FUND FOR FISCAL YEAR 2017

Before the
Committee of the Whole
Council of the District of Columbia

The Honorable Phil Mendelson, Chairman

March 7, 2018, 10:00 a.m.
John A. Wilson Building, Room 412
1350 Pennsylvania Avenue, NW
Washington, DC 20004

Testimony of
Jeffrey Barnette
Deputy Chief Financial Officer - Treasurer
Government of the District of Columbia

Good morning Chairman Mendelson and members of the Committee of the Whole. I am Jeffrey Barnette, Deputy Chief Financial Officer and Treasurer of the District of Columbia. I am pleased to testify on the FY 2017 performance of the Other-Post Employment Benefits Fund, hereafter referred to as the "Trust Fund" or the "Plan".

The Trust Fund's assets are used to pay health and life insurance benefits for participating District annuitants and the associated administrative expenses. The Trust Fund is administered pursuant to the Annuitants' Health and Life Insurance Employer Contribution Plan document.

As you are aware, Council legislation established the Other-Post Employment Advisory Committee ("Advisory Committee") comprised of external, independent subject-matter experts, who provide an additional level of oversight on important issues that can impact the performance and value of the Trust Fund, including actuarial assumptions, investment objectives and recommendations to achieve and maintain best practices. The last advisory meeting was conducted on January 9, 2018. At that meeting, we provided the Advisory Committee with a performance overview of the program and shared with them similar information in this testimony.

As of September 30, 2017, the Trust Fund was valued at $1.366 billion and had 1498 beneficiaries participating. For comparison, the program was valued at $1.197 for FY16. The Trust Fund's investment portfolio had a rate of return of 11.98% over the past fiscal year. For comparison, the benchmark policy index had a rate of return of 10.65% in FY2017. The Trust Fund had a return of 5.09% for the three-year period and 7.51% for the five-year period. The actuarial rate of return remains at 6.5%.

Considerable effort has been taken over the past few years to ensure that the investments, actuarial analyses and all other necessary elements are in place to ensure the Trust is funded at a level that provides for the District's' cost portion for annuitants' health and life insurance needs.

A plan's "Funding Ratio" is the ratio of the value of plan assets to the actuarial accrued liability at a point in time. A plan is considered fully funded when it has a funding ratio between 90% and 120% as of the date of the actuarial analysis. The funding ratio that was published in the FY17 CAFR was 111.57%.

Also, due to accounting standard changes, this figure is likewise presented in terms of dollars and that dollar value is equivalent to a net asset of $141.7 million. We continue to be a fully funded program.

As you know the District is in a unique position where employees hired before 1987 fall under the civil service retirement plan and receive retiree health benefits through that federal program. The Trust Fund was established to pay for health benefits for employees mostly hired after 1987 and the initial modeling assumptions for participation rates were very conservative to ensure the Plan was appropriately funded.

We have also made changes to the actuarial assumptions by adjusting the amortization period from a 30-year closed to a 20-year closed and adjusted the target rate to 6.50%. The amortization and return assumption changes currently match those of DCRB. The plan has also incorporated a 5-year smoothing of asset values, which also matches assumptions used by the D.C. Retirement Board ("DCRB). The prior and current actuarial work are used to determine the annual required

contribution (ARC). For FY17, the ARC was $31 million and the FY18 ARC is $44.5 million. Our actuary is currently completing the most recent study based on 9-30-2017 data and we will provide those results as input to the current budget process. The study will only impact the FY19 and future year budgets. Also, the name convention for the ARC will change and will be known as the Annual Determined Contribution (ADC). This is all part of the most recent GASB accounting changes.

We would like to share with you some additional information on the Plan's program.

One of the most significant projects associated with the program was the transition to a new custodian. We moved the plan assets from State Street Bank and Trust Company to The Northern Trust Company ("Northern Trust") on May 1, 2017. We have been pleased with the relationship so far and hope that their services will help us improve in our reporting and analytics. Northern Trust is also the current custodian for DCRB.

The Office of Finance and Treasury works directly with our investment consultant, Segal Marco Advisors (Segal), to constantly review the performance of our investment managers. Segal also works with us to determine the proper asset allocation to achieve the Plan's investment return target. The goal of the allocation is to provide the best risk adjusted returns. Last year, we did not make any allocation changes.

Although the District's Trust Fund is well-funded, we continue to review the Trust Fund's program to ensure it not only meets best practices but exceeds them, which is consistent with one of the OCFO's goals of continuous improvement. We provided and will continue to provide an annual report to the Mayor, Council and

the public that includes: Trust Fund information, the audited financial statements, Plan performance, and actuarial information.

Lastly, to ensure all aspects of the program are reviewed, we have engaged our actuary to perform an experience study. Specifically, we will closely review the participation rate of the Plan to make sure it aligns with the modeled participation assumptions. We will continue working with DCHR, the Advisory Committee and the actuary to make sure we have the most appropriate model.

In summary, the Trust Fund is in excellent shape. Our goals are to become more transparent, improve oversight of the plan and ensure that the Trust Fund is managed using best practices.

This concludes my remarks. I would be pleased to answer any questions you may have.