Town of Coventry
Pension & Retirement Committee
February 3, 2021

1. **Call to Order**: The meeting was called to order at 7:01 pm. Present were: Robert Murzyn, Ben Emanuele, David Powers (Zoom) and Cara Revett (via Zoom at 7:10pm). Also present were: Amanda Backhaus, Finance Director; John O'Connor, 3D Asset Management and Ben Lavine, 3D Asset Management (via Zoom); Richard Sych, Hooker & Holcombe.

2. **Approval of minutes:** Motion made Ben by to approve the minutes from October 28, 2020. Motion seconded by David and passed unanimously.

3. **Review of Current Holdings:** John began the discussion. He noted the quarter ended on high note. There was a small drop at the end of the third quarter. We finished the 4th with almost 11 million dollars. At this moment, we are over $11 million. There has been a lot of volatility in the market currently. Overall, they are happy with the plan's performance. Since Coventry chose to stay the course – we have regained a great deal of the value that had previously been lost.

   Ben Lavine continued noting that DFAs performance sky rocketed right after the election. He noted that when Pfizer and Moderna announced their efficiency rates in vaccination, it opened the door for some expectation of normalization in 2021. With that said, we are in the middle of second wave of outbreaks and several variations so it is uncertain how that will play out. Currently the market narrative is tug of war between COVID high positivity rate versus the promise and potential of vaccinations. We saw the steepest treasury yield curve that was have seen since 2016 which is related to the net positivity rate dropping below 4%.

   David asked what the 10 year moved to. Ben noted this morning it was over 110. Ben noted last week with concerns of the COVID variants, the curve had flattened to just around 1% but it has gone up quite a bit. Ben noted the treasury market is also influenced by what is happening in Washington in relation to COVID and prospects of a potential COVID relief.

   Dave asked if the fed had raised their expectations regarding inflation. Ben noted the dot plot forecast is still holding to zero rates through 2022. Ben noted at the Feds press conference in January, Powell used the word transient multiple times - setting expectations that uptick in inflation should be interpreted as transient. A steeper yield curve should benefit us in our small cap and value funds.

   John mentioned that there were changes to the plan's positions in January. We are trimming back to manage risk on small cap and foreign exposure. We are moving all DFA portfolios a little closer to their benchmark to make sure they are well positioned through the end of the year. Ben noted we are still tilted toward small caps but we trimmed down our position in micro caps and small caps on the international side. These have been moved back into the large cap market.

John noted the rate on the Town's GIC is still doing well and giving immunity to the volatile rate we are seeing currently. Between that and the growth in the equity fund, Coventry is in a good position for half way through the fiscal year. Dave asked if the interest rate really was volatile or if it could be classified as slowly rising. Ben noted it is very slowly rising but there was some volatility right after the Georgia Senate run off.

Ben noted they had also sent around the year-end commentary which also has an outlook. Also included is their long-term capital market projections which are helpful to temper expectations long-term. Ben spent time going over the different long-term calculations and how they were calculated.

Robert asked if other Towns are shifting away from the 60/40 allocation. Ben said 60/40 is still typical. Some Towns might be slightly more aggressive depending on their funding ratio. John noted many Towns are still working towards lowering their investment rate of return to more realistic ranges. Everyone thanked John and Ben for attending.

Amanda reviewed the pension asset summary and allocation, noting that in December the plan was at more of a 35/65% split. Robert noted it is a difficult decision, especially since the last time we did not rebalance the fund dropped significantly. Ben noted he was inclined to leave the funds as is until the next meeting unless something radical occurred. He noted we could hold a special meeting if need be. Cara agrees with Ben. Dave likes the 65/35. Cara asked if we should set a threshold if we drop to a certain level if it goes down. Ben noted that would rebalance. Bob agrees to leave as is until the next meeting.

The Committee reviewed the GL reports. No additional questions were noted.

4. **Retirement review:** Amanda noted there were no retirements to review.

5. **July 1, 2020 Actuarial Valuation:** Richard began his presentation. He started with an overview of the valuation process. They collect the data as of July 1 and then reconcile with last year to get a new database. Then the plan is programmed into their system. They project active employees to retirement, including probability of turnover, retirement, salary increases and death. They then estimate the benefits at retirement and how long the benefit will be paid. Ben inquired if this automatically adjust at higher and lower rates based on the market swings. Richard said no, the valuation is only a snapshot as of July 1.

   Once we have cash flows schedule, Richard noted they then discount this back to today. When calculating the liability, the most assumption is the rate of return. Others also important, turnover, retirement, salary increases, but the investment return rate is much more significant.

   Richard went over the plan demographics, noting that lump sum options are still available for many participants.

   Richard reviewed the asset returns for the last 5 years, including market value versus actuarial value which is averaged over 4 years to help smooth contributions.

Richard moved on to the target allocation. There is a required to disclose the pension liabilities and support for investment return assumption. Richard noted that he worked with Amanda, Ben and Bohn for the expected real rates (in excess of inflation) and the target allocation. The expected real rate is 4.21%. Then add inflation of 2.4% (used by social security administration) to get to 6.61%. 6.61% does not reflect rebalancing or changes in assets. He noted you could add 50 basis point of alpha in which case you get to about 7.1% for expected rate of return in the future. This rate goes out to the last payment of the youngest person which is a very long time and is most impactful to the calculation.

Richard noted the valuation must be in line with the expected rate of return. He outlined changes in assumptions from this year to last year:

- Pre-retirement was lowered to 7.25% and post-retirement to 6.9%. He noted that 7.25% is a challenging rate to support to Moody's or S&P based on 6.61% in the actuary report.

- Simplified post retirement to 6.9%. Average is 7.1% – which is close to the 7.1% noted in the previously paragraph. Averages are under 7% for CT municipalities if they were to be surveyed.

- Salary increases and

- An updated mortality table from MP-2019 to MP-2020. This table is specific to municipalities and is the most current up to date table.

Richard then discussed the contribution calculation, which includes funding the normal cost plus 15-year amortization of unfunded plus benefits accruing. They then compare this to the value of the plan assets to get the funding ratio.

Rich noted that based on the actuarially determined liability and plan assets, the funding ratio decreased. Rich noted it is comment to expect to be higher on the liability side when you lower your investment return assumption. That is the primary driver for the increase. The losses that were occurred in the plan year have not yet recognized in actuarial valuation due to the 4 year smoothing of asset value.

Rich mentioned the GASB 67/68 report which provides the information for the Town's CAFR. The terminology is slightly different but drilled down it is the same thing. GASB does not let you smooth assets – you must use market value as of reporting date. He noted the snapshot of market was weak as of June 30, but it is important to remember that it is a snapshot.

Dave asked Richard, if as an actuary, do you feel these pensions ever need to be fully funded? Richard says he likes well-funded plans. Every plan will eventually be fully funded because they must make all payments to participants. Many agree there is no reason to fully fund. One reason to fund is for generational equity – you do not want to make the current generation pay for the benefit that has already been accrued. S&P and Moody's like to see around 80% for a funding ration.

Kara asked, as we think about projections and experience of last year, how does that feed into the numbers and assumptions? Is there any negative impact? Or do we ignore it because it is an anomaly? Richard noted that the pandemic is definitely having an impact. He noted that projection/mortality tables are updated each year. As COVID data starts entering the data for mortality, his expectation is that the new tables will include shortened life expectancy, which will result in means lower liabilities. Dave thinks that impact will be miniscule. Richard agrees due to lack of data and that it might be a few years before we see the full impact.

Ben stated that he understands smoothing and that long-term projections are meant to help avoid blips. Is anything being done on the asset side to deal with the extraordinary circumstances and balances? Richard said that would be a question for 3D. Hooker and Holcombe uses 4 year average. This could be changed to 5 but we would need to talk to Ben Lavine and John about changing to a 5 year smoothing if you're expecting volatility. Ben is concerned about the shift in the assumed rate of return, although not opposed due to the current changes in market conditions), and the extreme underperformance in the past year will affect the overall recommendation in making the ADEC. Richard noted that now that the investment return is 7.25% rather than 7.5%, this will help with the gains/losses of the smoothing as well.

The Committee thanked Richard for the detailed presentation.

Amanda noted that the current FY22 budget included the contribution that was recommended by the actuary. Bob noted the Committee should make a recommendation to Town Council for upcoming FY22. Dave said we don't have to fully fund it and is not in favor of full contribution. Cara agrees with Dave. She is uncomfortable with change in rate of return and now the liability is greater. Ben noted it is inevitable but will be more of a strain on the tax payer. Cara did note we are now below 80% and we should get to that level. Ben noted if you look at rough numbers currently (rather than at June 30) compared with a small increase in liability – you then get a number in excess of 80%. Ben knows we have no idea what will happen when market rebounds and potential infrastructure is not able to handle it. Ben thinks we won't know until a year or two what will really happen. Bob noted recommendation per report is $892k. Motion to make recommendation to contribute equivalent to last year's valuation made by Dave. Dave mentioned again we do not need to be fully funded. Motion seconded by Ben. Motion passed unanimously. Bob Clarified $724,037 equivalent to prior year.

6. **Other Business:** Cara asked administratively, how do we change rate of return? Also that perhaps next year the pension committee could be notified next time. Amanda noted there was no time this past year. The change in the rate of return was not optional due to actuary not being able to support the rate. Justifiably, we should have gone even lower. Ben mentioned if the actuary said the rate needed to be changed then there was no option. Amanda noted that next time she can attempt to include the Committee in further discussion on the actuarial valuation and interest rate assumption. Motion made by Dave that in future discussions with the actuary regarding actuarial assumption the Committee should be

consulted and brought in as part of discussions. Second by Cara. Motion passed unanimously

7. **Adjournment:** A motion was made to adjourn the meeting by Cara at 8:38 pm. Motion seconded by Ben and passed unanimously.

Respectfully Submitted,

A.L.B

Amanda L. Backhaus, CPA

Finance Director

Note: These minutes are draft/not official until approved by the Committee at the next Committee meeting. Please see subsequent meeting for approval or changes to these minutes.