State of Alaska
ALASKA RETIREMENT MANAGEMENT BOARD
ACTUARIAL COMMITTEE MEETING

Captain Cook Hotel – Club Room II
939 W. 5th Avenue
Anchorage, Alaska

October 4, 2017

ATTENDANCE

Committee Present:	Kristin Erchinger, *chair* Tom Brice Gayle Harbo Rob Johnson Acting Commissioner Leslie Ridle Norm West
Committee Absent:	Commissioner Sheldon Fisher Bob Williams

Department of Revenue Staff Present:
Bob Mitchell (chief investment officer)
Pamela Leary (director, Treasury Division)
Zach Hanna (deputy chief investment officer)
Shane Carson (state investment officer)
Stephanie Alexander (board liaison)

Department of Administration Staff Present:
Ajay Desai (director, Division of Retirement & Benefits)
Kevin Worley (chief financial officer, Division of Retirement & Benefits)

Others Present:
Scott Young (Conduent Human Resource Services, actuary)
David Kershner (Conduent Human Resource Services, actuary)
Paul Wood (Gabriel Roeder Smith & Company, review actuary)

I. CALL TO ORDER
CHAIR ERCHINGER called the meeting to order at 10:22 a.m.

II. ROLL CALL
Five committee members were present to form a quorum. Acting commissioner Leslie Ridle arrived at 10:56 a.m.

III. PUBLIC MEETING NOTICE

Board liaison STEPHANIE ALEXANDER confirmed that public meeting notice had been met.

IV. A. APPROVAL OF AGENDA

MS. HARBO moved to approve the agenda. MR. JOHNSON seconded. The motion passed without objection.

B. APPROVAL OF MINUTES – June 21, 2017

MR. BRICE moved to approve the minutes of the June 21, 2017 meeting. MR. WEST seconded. The minutes were approved as presented.

V. PUBLIC/MEMBER PARTICIPATION, COMMUNICATIONS AND APPEARANCES

No one present at the meeting or listening by telephone indicated they wished to speak to the committee. MS. ALEXANDER stated that she had received no communications for the committee.

VI. A. Discussion on FY2019 PERS/TRS/JRS Additional State Contributions

MR. WORLEY, Chief Financial Officer in the Division of Retirement & Benefits, introduced DAVID KERSHNER and SCOTT YOUNG of Conduent Human Resource Services, the State's actuary.

MR. KERSHNER referred to a two-page letter from Conduent to the Division of Retirement & Benefits (DRB) dated September 15, 2017, with two exhibits attached, which was included in the meeting packet. The letter confirmed the setting of the fiscal year 2019 employer contribution rates and the additional state contributions for the Public Employees' Retirement System (PERS), Teachers' Retirement System (TRS), and Judicial Retirement System (JRS). He briefly reviewed the process for calculating the FY19 PERS and TRS contribution rates and additional state assistance. A couple of years ago the process was modified so that for FY17 Conduent used the actual investment earnings and benefit payments taken from the financial statements. The second year of the projection is still on an expected basis, where assets and liabilities are projected based on the expected 8.0% investment return and expected benefit payments and accruals.

MR. KERSHNER noted that Exhibit 1 in Conduent's letter allocates the state additional contribution between pension and healthcare based on their respective unfunded liabilities. Exhibit 2 was introduced a couple of years ago when the committee made a decision to allocate 100% of the state assistance contribution to pension.

MR. KERSHNER stated that the projected unfunded liability at 6/30/18 for the two-year roll-forward for PERS was approximately $6.1 billion. Because the investment return was about 13.25% in fiscal year 2017, which exceeded the 8.0% expected return, the expected unfunded liability is now around $5.7 billion. The fact that assets earned more than the return target does not hit the contributions immediately because of the asset smoothing, so only 20% of the asset gain is recognized in the current year. The PERS assets are about

$750 million more than the actuary expected them to be at 6/30/17, and for TRS the assets are almost $400 million more.

The total PERS defined benefit plan (DB) and defined contribution plan (DCR) contribution rate is 27.58% (22.64% of which is DB). The PERS employer contribution rate is capped at 22.0%, so the excess 5.58% is the additional state contribution. The dollar amount of the additional state contribution for FY19 is about $23 million less than it was projected to be because of the favorable asset performance during the year.

The total TRS defined benefit plan (DB) and defined contribution plan (DCR) contribution rate is 28.90% (the DB portion is 23.56%). The TRS employer contribution rate is capped at 12.56%, so the additional state contribution to the defined benefit plan is 16.34%. The dollar amount of the additional state contribution for FY19 is about $12 million lower than projected because the investment return on assets was better than expected.

MR. WORLEY stated that the discussion on allocating the additional state contribution between pension and healthcare will be saved until after everyone sees the next valuation reports.

CHAIR ERCHINGER said that despite the tremendous unfunded liability in the Alaska plans, people can at least take heart in knowing that Alaska has done a better job of funding healthcare than most other states have. She was curious about the estimated impacts of showing the unfunded healthcare numbers on the employer financial statements.

MR. KERSHNER replied that it was too soon to say because Conduent is still in the process of collecting data from Aetna (the third-party administrator of the Alaska health plans) that is needed to analyze how things have performed in the last year.

B. FY2019 Employer Contribution Rate Review

Information: History of PERS/TRS Employer Contribution Rates

CHAIR ERCHINGER referred to the one-page chart of the PERS and TRS employer contribution rates for fiscal years 2010 through 2018, and including the proposed FY19 contribution rates. She said the committee would be considering the proposed rates for the PERS DB employer contribution, the DCR retiree medical plan, the occupational death and disability for all others, and the occupational death and disability for police and fire. For TRS, the proposed rates for consideration were the DB employer contribution, the DCR retiree medical plan, and the occupational death and disability.

Staff had provided a summary memo attached to each of the contribution rate resolutions.

MR. JOHNSON asked the Conduent representatives if they could confirm and concur that the figures in the history of ARMB adopted contribution rates in the one-page chart, including the proposed contribution rates for FY19, were accurate. He asked further if any of the figures had a different level of certainty as to their accuracy.

MR. KERSHNER stated that Mr. Worley had sent him the one-page chart, and he had reviewed and confirmed all the rates with Conduent's valuation reports and the letter he had talked about earlier. His certainty about the accuracy of the rates applied specifically to the current year that the committee and the ARMB were going to adopt, because he did not verify all numbers going back several years.

CHAIR ERCHINGER said the committee assumed that the PERS employer contribution and state assistance above 22% was based on the 6/30/2016 valuation rolled forward, and that Conduent's review was reviewed by Gabriel Roeder Smith as well.

MR. YOUNG stated that he reviewed the rates, and everything was consistent with the valuation report and with the letter dated September 15, 2017. The only issue he noted was that in the actual resolutions all the numbers are consistent with Exhibit 1, allocating the state assistance based on the past service for the unfunded liability amount. He wanted the committee to be aware that that was written into the resolutions.

CHAIR ERCHINGER thanked him for that clarification. She noted that Mr. Worley had indicated that Exhibit 2 would be helpful for next year if the committee decided to allocate instead to pension and not base the allocation on the proportionate share of the unfunded liability.

Action: Relating to FY19 PERS Contribution Rate - Resolution 2017-06
<u>MR. BRICE moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set the Fiscal Year 2019 PERS actuarially determined contribution rate attributable to employers, consistent with its fiduciary duty, as set out in the attached form of Resolution 2017-06.</u> <u>MR. WEST seconded</u>.

CHAIR ERCHINGER entered a paraphrased portion of the last paragraph of the resolution into the record, as follows: "…that the FY2019 actuarially determined contribution rate attributable to employers participating in PERS is set at 27.58 percent, composed of the contribution rate for defined benefit pension of 18.27 percent, the contribution rate for postemployment healthcare of 4.37 percent, and the contribution rate for defined contribution pension of 4.94 percent."

Without objection, the motion passed, with committee members Erchinger, Brice, Harbo, Johnson, and West present.

Action: Relating to FY19 PERS DCR Retiree Major Medical Insurance Contribution Rate - Resolution 2017-07
<u>MR. WEST moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set Fiscal Year 2019 PERS DCR Retiree Major Medical Insurance rates as set out in the attached form of Resolution 2017-07</u>. <u>MR. BRICE seconded</u>.

CHAIR ERCHINGER stated that Resolution 2017-07 sets the fiscal year 2019 employer contribution rate for the retiree major medical insurance for PERS defined contribution plan at 0.94 percent.

There was no discussion. The resolution was approved with five committee members present.

Action: Relating to FY19 PERS DCR Occupational Death & Disability Benefit Contribution Rate - Resolution 2017-08
<u>MS. HARBO moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set Fiscal Year 2019 PERS DCR Retiree Major Medical Insurance and Occupational Death & Disability Benefit rates as set out in Resolution 2017-08</u>. <u>MR. JOHNSON seconded</u>.

CHAIR ERCHINGER stated that Resolution 2017-08 sets the FY19 employer contribution rate for PERS occupational death and disability benefit rate at 0.76 percent for peace officers and fire fighters, and at 0.20 percent for all other PERS defined contribution retirement plan employees.

Without objection, the resolution was approved with five committee members present.

Action: Relating to FY19 TRS Contribution Rate - Resolution 2017-09
<u>MS. HARBO moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set the Fiscal Year 2019 Teachers' Retirement System actuarially determined employer contribution rate attributable to employers, consistent with its fiduciary duty, as set out in the attached form of Resolution 2017-09</u>. <u>Seconded by MR. JOHNSON</u>.

CHAIR ERCHINGER noted that Resolution 2017-09 establishes the FY2019 actuarially determined contribution rate attributable to employers participating in the Teachers' Retirement System at 28.90 percent, comprised of the contribution rate for defined benefit pension of 20.86 percent, the contribution rate for post-employment healthcare of 2.70 percent, and the contribution rate for defined contribution pension of 5.34 percent.

The motion carried without objection or discussion, with five committee members present.

Action: Relating to FY19 TRS DCR Retiree Major Medical Insurance Contribution Rate – Resolution 2017-10
<u>MR. BRICE moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set Fiscal Year 2019 Teachers' Retirement System DCR Retiree Major Medical Insurance rates as set out in Resolution 2017-10</u>. <u>Seconded by MR. WEST</u>.

For the record, CHAIR ERCHINGER declared that the resolution provided for setting the FY2019 employer contribution rate for the retiree major medical insurance for the Teachers' defined contribution retirement plan at 0.79 percent.

There was no discussion or objection, and the motion to approve was unanimous.

Action: Relating to FY19 TRS DCR Occupational Death & Disability Benefit Contribution Rate - Resolution 2017-11

MR. WEST moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set Fiscal Year 2019 TRS DCR Occupational Death and Disability Benefit rates as set out in Resolution 2017-11. MR. BRICE seconded.

CHAIR ERCHINGER stated that Resolution 2017-11 established the FY2019 employer contribution rate for the TRS occupational death and disability benefit rate at 0.08 percent for all Teachers' defined contribution retirement plan employees.

Without objection, the resolution was approved with five committee members present.

Action: Relating to FY19 National Guard & Naval Militia Retirement System (NGNMRS) Contribution Amount - Resolution 2017-12

MS. HARBO moved that the Actuarial Committee recommend that the Alaska Retirement Management Board set the Fiscal Year 2019 NGNMRS annual contribution amount, consistent with its fiduciary duty, as set out in the attached form of Resolution 2017-12. Seconded by MR. JOHNSON.

CHAIR ERCHINGER stated that Resolution 2017-12 establishes the FY2019 contribution amount for the State of Alaska, Department of Military and Veterans' Affairs to the Alaska National Guard and Naval Militia Retirement System at $851,686.

There was no objection, and the resolution was passed and approved, with five committee members present.

CHAIR ERCHINGER clarified that the committee's actions do not approve the contribution rates. The committee, in passing the resolutions, was making recommendations to the full Board to approve those rates.

Information: Judicial Retirement System Contribution

CHAIR ERCHINGER referred to the informational memorandum in the packet regarding the FY19 employer contribution rate of 70.24% for the Judicial Retirement System (JRS). The Commissioner of Administration is the party responsible for establishing a rate for the JRS. Conduent calculated the rate based on the actuarial valuation of the Alaska Judicial Retirement System as of June 30, 2016. The pension portion of the rate is 70.59%.

MR. WORLEY explained that the Judicial post-employment healthcare plan is in an overfunded status currently. (The normal cost rate for healthcare is 4.47%, with a credit of 4.82%, which made for a zero contribution for healthcare).

MR. WORLEY said that the Alaska Court System operating budget uses the normal cost rates for each of the plans: 38.14% is funded on pension, and 4.47% on healthcare. The total is a 42.61% contribution rate. The remaining amount of $4.9 million (or 32.45%), as shown on page 2 of the Conduent letter, comes in the language section of the operating bill. The past service cost amount is not in the Court System's budget.

MR. KERSHNER mentioned that all the contribution rates just acted on reflect the decision the committee made a meeting or two ago to contribute the normal cost as a minimum.

CHAIR ERCHINGER introduced the Acting Commissioner of the Division of Administration, Leslie Ridle, who had joined the meeting.

C. Experience Analysis Study - 2018

Health Care Cost Trend

[Conduent's slide presentation dated October 4, 2017 is on file at the ARMB office]

MR. KERSHNER stated that Conduent had discussed the concepts regarding the economic assumptions at the June meeting. They have not completed the experience review and did not intend to recommend any assumptions at this meeting. In fact, they are still working through the census data for the 6/30/17 valuation, which will form the last year of the four-year experience period. Today's presentation was to complement what they did in June and to present assumptions that are specific to healthcare.

MR. KERSHNER tied in the experience review to the overall valuation process by saying that the experience is looking at the actuarial assumptions and the funding methodology every four years. The actuary analyzes the experience and compares it to what it is expected to be, and how assumptions should be adjusted looking forward, based on the most recent four-year period. Once any new assumptions are adopted by the Board, Conduent will use them beginning with the 6/30/18 valuations. Each assumption has to be a realistic best-estimate of that assumption based on its past history and future expectations. It is not allowed to include some conservatism here and maybe less conservatism somewhere else.

MR. YOUNG briefly reviewed the particulars of the actuarial standards of practice that actuaries are bound by, similar to the ASOP 27 standards that the committee heard about as part of the presentation on economic assumptions at the last meeting *[slide 8]*.

CHAIR ERCHINGER referred to the bullet point "that the actuary should not give undue weight to recent experience." She thought that recent experience would necessarily deserve a higher weighting.

MR. YOUNG stated that the retirement funds had a 13-plus percent return on assets in the prior year. The expected investment return is 8.0%. The statement the Chair cited means not to expect to earn 13% again next year. In the healthcare plan, if claims were flat or went down 2%, it does not mean that will happen again, and the ARMB would still want to go back to its best-estimate assumption of what claims will be next year.

Continuing with the same example, CHAIR ERCHINGER responded that if claims were trending in that direction, then the actuary would take into account that the trend was upward or downward.

MR. YOUNG confirmed that she was correct.

MS. HARBO voiced her opinion that the inflation assumption has been fairly high for the last few years and should be looked at.

MR. KERSHNER said that Conduent was definitely evaluating the inflation assumption.

CHAIR ERCHINGER recalled that the payroll growth assumption was set at zero percent in the short term for setting the previous contribution rates. She said she did not know what that does to the long-term projections, given Alaska's budget problems and hiring issues right now.

MR. KERSHNER clarified that the zero percent was on the population growth assumption. There is still a long-term payroll growth assumption that is currently comprised of 3.12% inflation and 0.5% for productivity, for an overall number of 3.62%. Conduent's recommendation will probably be to lower the 3.12% inflation number.

CHAIR ERCHINGER remarked that everyone she talks to is eliminating positions, so she felt the payroll growth assumption was overshooting.

MR. YOUNG stated that in the experience study Conduent will be looking at balancing an assumption being very refined or detailed versus being material. For example, an assumption may be appropriate for one percent of the population, and it takes a lot of work and effort to get that really refined. But for valuation purposes, Conduent may be able to take a broader assumption that applies to everybody. And it is just a slight weighting difference from that one percent versus everyone else that gives an equally accurate overall valuation result and makes a complicated process perhaps a touch less complicated.

MR. YOUNG also mentioned ASOP 6, another actuarial standard of practice that was materially updated in 2014. The biggest change does not affect Alaska because it changed community rated plans. What does impact the ARMB is the prescribed assumptions – those set by law or another party. The actuary's responsibility is to evaluate those, to the extent that they can, and if they are reasonable, then go ahead and use them and state that they are reasonable. Or the actuary can state that it was not within the scope of their services to evaluate the assumption, and they go ahead and use the prescribed assumption. If a prescribed assumption is unreasonable, the actuary can state that and still use it for the valuation. ASOP 6 guides the actuary on what they need to disclose and communicate when doing the work on assumptions that are outside of their control.

MR. YOUNG explained that ASOP 6 also deals with the trend rates and many of the factors that go into setting them. It is a complicated assumption because the actuary is trying to look at what they expect the healthcare costs to be over the next one hundred years, and it is not an easy thing to predict. The actuary looks at what they know about other plans of the same type over the near term. For the last 20-plus years that he has been doing valuations like this, everyone assumes that the current cost increases are at whatever level they are, and the costs are expected to climb over time to reach some ultimate long-term rate. It seems that every year those high rates keep pushing forward and they never seem to materialize. Besides the near-term expected changes in the trend rate, Conduent looks at (1) how long they expect those to occur over time; (2) the retiree contribution changes for the defined contribution plan group; (3) adverse selection, where if participants have to pay a high percentage of the cost they start dropping out, and only the sicker people remain in the health plan; (4) morbidity/aging, which addresses how the costs vary by age groups of retirees compared to the current assumption; and (5) large studies over multiple years that show how much costs vary by age, in order to give an accurate, long-term cost projection.

MR. JOHNSON asked if Conduent was expecting new life-expectancy tables to come out in the near future. He recalled that about 20 years ago the ARMB's predecessor board was surprised by the last-minute delivery of a significant change in life-expectancy calculations.

MR. KERSHNER stated that the Society of Actuaries published the most recent industry standard tables in 2014, along with generational mortality improvement, which recognizes that every year people are going to live longer and longer. Those tables are based on hundreds of thousands of lives experience that were collected. The Society of Actuaries collected data for private plans and public plans, and it discarded the public data because they felt that the experience was not consistent with the private plan data. Private plans and public plans often exhibit different behaviors. The Society is currently studying a public-sector-specific mortality table that will be comparable to the tables issued in 2014, but the issue date is unknown. Conduent will definitely be updating the mortality assumption that has been used for the last four years to include some sort of generational mortality improvement. If there is no public sector standard table published by the time Conduent needs to set the assumptions, they may, by default, go to the tables that were published for the private sector in 2014. The new mortality assumption will definitely be reflecting increased life expectancy, and that will mean higher liabilities and lower funded status, all other things being equal.

MS. HARBO mentioned that most of the Tier I retirees are over 65, so they are enrolled in Medicare, and Medicare pays primary on claims. She thought there were about 450 Tier I employees left to retire. The healthcare costs should go down significantly for the defined benefit plan people because most of them are Medicare age.

MR. KERSHNER stated that the mortality table focuses on how long those people are expected to generate healthcare costs.

MR. YOUNG next addressed the healthcare cost trend assumption, which he said is a very significant assumption, particularly for plans that do not have a cap or some other way to limit costs. The healthcare cost trend is the change in average health claim and administration costs over time. In order to get the present value of the retirement funds correct, Conduent has to project all those future costs out into the future and then discount them back to the present day to get a value for the obligation. It is a complicated assumption because it takes into account the current costs, what the costs are expected to be in the future, how the plan design might change, and any other factors that might impact costs in the future. Three or four years ago prescription drug costs were increasing a lot slower than they have been recently because of new innovations in things like hepatitis-C treatments and biological drugs. Prescription drug trends are now double-digit percentage increases, and that really affects the healthcare cost trend.

MR. YOUNG said the State of Alaska uses the Getzen model to project out how long the medical cost trend will be long-term and what pattern it will be.

MR. MITCHELL stated that the defined benefit plan health plan booklet that was amended in 2016 indicates that prescription drug expenses have a two-million-dollar lifetime cap. He asked if that cap was being captured in Conduent's forecast for healthcare liabilities.

MR. YOUNG said not explicitly, because $2 million is such a high cap, and there is little chance that enough retirees would hit the cap to really matter. The current average prescription drug cost per person is $3,320 per year.

MR. KERSHNER noted that it would be reflected in the experience study. If an individual were to hit the $2 million cap in prescription drug expenses, the insurance company would stop paying claims on their behalf, so the claims experience would reflect the imposition of that cap. Other than that, the cap is not reflected in Conduent's projected trends.

MR. YOUNG provided more background on the Getzen model that Conduent uses as a tool to project the expected growth in healthcare costs from the current year to one hundred years later *[slide 14]*. He said that at some point healthcare costs cannot keep growing as fast as they have been or it will consume so much of the economy that everybody will be working in healthcare. The model tries to project out to a point where one can assume that healthcare only reaches a certain percentage of the total GDP (gross domestic product). At that point, the increases have to convert back to whatever overall inflation and GDP are increasing by. For the Alaska plans, pre-Medicare eventually reaches a 4.4% ultimate trend, and post-Medicare ends at a 4.0% trend. Conduent will give the model some inputs for what they think the next five years of trend to be. Then some other parameters will go into the model, and it will project what to expect the pattern of trend rates to be over the life of the plan. That will be the basis for setting up the healthcare cost trend assumption.

MR. PAUL WOOD of Gabriel Roeder Smith (GRS) said he had heard that healthcare in Alaska is a much different animal than it is in other places because there is not a lot of access to care and providers have people over a barrel. He asked what local factors Conduent would work into the Getzen model to take that into consideration.

MR. YOUNG indicated that he was new with the Alaska plans, so he would have to talk with people who have more experience with the current actual provisions and take that into account in the experience study. He had heard from Melissa Bissett, for example, that some retirees live a significant portion of their time outside of Alaska, so they may have very low costs because they are not in the state that often.

MR. YOUNG displayed a table *[slide 15]* that showed the current average healthcare cost per person in the plan for FY17, depending on if they are pre-Medicare, or enrolled in some combination of parts of Medicare. The healthcare trend assumption calculates what the average healthcare cost will be in the next year for each group. That process continues for every future year, using the assumption for each year of the trend. Prior to Medicare age is the highest cost because Medicare is not there to be the primary payer to offset the cost. Once a person in the plan becomes eligible for Medicare, the average healthcare cost drops significantly.

MS. HARBO asked if the prescription drug side of Conduent's table took into account the federal drug subsidy the State of Alaska receives quarterly.

MR. YOUNG pointed out the Medicare Part D line that showed a $647 per person offset to the cost for the State.

MR. YOUNG moved on to demographic assumptions – what the demographics of the population are going to do and how these assumptions affect them. The first was the morbidity assumption, which determines how the healthcare cost varies by age. All studies have shown that costs do vary by age for various reasons. The experience study will look at that for the Alaska retirement plans' most recent experience to see how that compares to the most current assumption and whether it warrants any change. Another option to consider is to look at the population as healthy or disabled. He personally would not look at that too closely because generally disabled populations are not that big and do not provide enough data to come up with a credible assumption. Also, the Alaska plans do not currently make that distinction.

Gender is another common consideration that some plans use for the morbidity assumption. Currently, the State does not use a gender-specific morbidity. There are studies (one by the Society of Actuaries) that show that a male and female the same age definitely have different average healthcare costs.

Medicare eligibility is another demographic consideration on the list, but Conduent was not necessarily suggesting using it.

MR. YOUNG stated that the Alaska plans have different assumptions for medical and prescription drugs. The ARMB could keep that distinction or add a gender component to it as well.

MR. JOHNSON asked why the plans have not had a gender distinction if there is a factual difference in the average healthcare costs for males and females.

MR. YOUNG indicated he did not know the history of that position. He added that the standard assumption that Conduent uses for most of their clients, and the one that was produced by the Society of Actuaries, does have a different assumption for males and females. Conduent received data from Aetna that is split out between male and female, and he was interested in seeing how that pans out for the Alaska group specifically.

MR. WOOD pointed out that the teacher population is probably heavily weighted toward females traditionally. If the assumption is not split by gender, it could result in a big shift in cost if there was a split between males and females. The curve is sort of interesting because the females are initially a little more expensive, and then they get through maternity age and become less expensive. The curve crosses over again where males end up being much more expensive at the tail-end. If the Alaska plans do go to a split assumption on healthcare costs, the State could see a fairly significant shift in costs.

MR. YOUNG stated that the next assumption is participation and coverage elections. This one is more relevant for the active employees. Conduent knows who in the retiree population participates and who their dependents are. For the actives, Conduent has to make an assumption for when they become eligible, when they retire, are they going to elect a plan, are they going to be married, are they going to cover their spouse, or are they going to cover any of their children. That can have a very big impact on the plan liability because, if someone is married, that is two people covered by the healthcare plan and twice the cost of the employee only. Conduent will look at the actual data over the last four years and see if the married percentages are still in line with the current 85% for males and 70% for females. Then the committee can decide if it wants to revise the assumption if Conduent sees a pattern. This is a case where not to give too much credence to the most recent experience, but to take into account if there is a pattern.

CHAIR ERCHINGER remarked that perhaps Alaska is unique in participation and coverage election area because of the small population, but a relevant question is whether a married employee is married to someone else in the healthcare plan. It is an important factor so the assumption is not adding a spouse on top of somebody else who is already in the plan, thus making the covered population larger than it should be. Ten percent of the Alaska plan population fits the duel coverage category.

MR. YOUNG said Conduent needs the data from Aetna in order to adjust the census data so they are not counting those people twice.

MR. YOUNG stated that currently there is a three-year age difference assumption, where it is assumed that a male active employee is going to be three years older than a female when they retire. This is a very common assumption across all plans. Conduent will look to see if the actual population is similar to that.

MR. YOUNG next talked about other considerations in setting the healthcare-related assumptions. He started with benefit design and plan provision considerations. In the experience study, Conduent will look at medical (participant cost-sharing and leverage), prescription drugs (cost-sharing by tier and federal rebates and subsidies), and administrative fees. Regarding leverage, he noted that when the cost of medical procedures goes up from one year to the next, and the plan participant continues to pay the same fixed deductible, the State pays a higher percentage of the cost because the plan design does not index with cost increases. That is a factor that will impact the trend assumption. Prescription drug costs have been going up at much higher rates than normal recently, so Conduent will look at that. They will also look at the prescription drug rebates the State is receiving and how those are expected to change in the near future.

Regarding administrative fees, MR. YOUNG stated that Conduent will examine the administrator contracts. According to the prior experience study, the current assumption is that contracts will increase 5% a year forever. He found that a higher percentage than he has seen elsewhere. If the ultimate assumption is around 4% for prescription drugs and medical, at first glance that seems to be a place where the 5% administrative fee increase assumption might be worth lowering, particularly because the companies that administer healthcare programs are very competitive. Aetna is not going to increase their third-party administrator contract 5% a year because they know that Anthem or UnitedHealthcare or Signa would be more than happy to come in and lower their fees and not increase them 5% a year.

There are definite differences between the defined benefit and defined contribution plan designs, so that goes into consideration for various assumptions. Medicare coordination method is also something very different between those two plans. The defined benefit plan has a standard coordination method, which is the most generous way that the plan coordinates with what Medicare pays. The DCR group has a different method, which is a lot less generous and ends up paying fewer dollars out of the plan than the DB group. Finally, there is a different subsidy between the Retiree Drug Subsidy (RDS) and Employer Group Waiver Program (EGWP) subsidy. Conduent understands that the DCR group will be going to the EGWP by January 2018, so they have to appropriately reflect that in the experience study.

MR. YOUNG mentioned that another consideration is retiree contribution increases, which is relative to the DCR group. He said that Conduent wants to make sure they understand how the retiree contribution amounts are developed and what the plan is for retiree contribution increases in the future. It is important that how those are developed is consistent with how Conduent is developing the per capita costs that are used to project the total costs. A disconnect would create a flaw in the model for projecting the future net cost to the State. Right now, the assumed increase in retiree contributions is at a different rate than the healthcare costs are. Conduent wants to reconcile those differences and make sure that the overall strategy for how contributions are going to change is consistent with the ARMB's intentions and with every other assumption within the valuations.

MR. YOUNG said that Conduent will be looking at dependent healthcare costs and premiums and how they are set, and if that will affect how employees decide whether or not to enroll their dependents. Some organizations do not want to subsidize as much for the dependents as they do for the retiree, so that could impact how many of those dependents would actually enroll in coverage if they have options elsewhere.

MR. YOUNG explained that "anti-selection" as a consideration in a retiree contribution increase means that, if healthcare costs are increasing at faster rates, then the people who stick around are more likely to be the ones who are generating higher costs.

MR. YOUNG briefly reviewed a list of Conduent's sources for relevant information *[slide 23]*.

ACTING COMMISSIONER RIDLE said that another unique aspect of Alaska is the Indian Healthcare Service. She did not know how many of the retirees were participants in that system or if they represented a higher percentage of the population in Alaska than in other states. She asked if that was considered as part of the experience study.

MR. YOUNG replied that Indian Healthcare Service participation among retirees certainly should be taken into account, and he would have to learn more about it.

D. Review of Experience Study Analysis and Valuation Timelines

MR. KERSHNER referred to the current schedule for the experience study, included in the meeting packet. Also included were two spreadsheets: the timeline for the experience study, and the timeline for the June 30, 2017 valuations.

Regarding the experience study timeline, Conduent, at the December 6 meeting, will be proposing recommended economic assumptions that cover both pension and healthcare. At the March 28, 2018 meeting, they will be reviewing the proposed demographic assumptions. Once those are recommended, Conduent will bring it all together and have a meeting with the committee, and ultimately the Board, to discuss/revise and adopt the assumptions that have been recommended. He noted that there are various touch points where Conduent will do their work, send it to GRS for the review actuary's analysis and review, then discuss GRS's findings and Conduent's responses before anything is presented to the committee.

MR. MITCHELL asked if the recommended investment return and inflation return assumptions would be presented at the December board meeting, and if Conduent would be using the ARMB's existing asset allocation policy.

MR. KERSHNER said they would use the new asset allocation that the Board just adopted.

MR. MITCHELL asked further if Conduent would consider an array of asset allocations to opine upon.

MR. KERSHNER indicated that they could, if the ARMB had an array of asset allocations it was considering.

MR. MITCHELL said he mentioned it because at the June meeting the Board adopted asset mix #4 of 5 mixes the trustees considered. Conceivably, each year the Board could be making a choice of various levels of risk or return expectation. It might be helpful to have the different return assumption numbers for the five different asset allocations, at least as a reference point in future years.

CHAIR ERCHINGER proposed amending the timeline for the experience study to include the ARMB approval of the assumption changes before the existing #26 on the timeline. She said the committee will be talking about the economic assumptions at one point and demographic assumptions, but she did not think it was reasonable to expect that in the same meeting the committee will be ready to act upon the recommended assumptions and recommend them to the Board.

MR. KERSHNER explained that Conduent meant that the June 20 committee meeting was to finalize the assumptions and then make a recommendation to the Board the next day.

CHAIR ERCHINGER requested that the timeline specifically indicate the meeting when the Board would be expected to act on the committee's recommendations, so it would not miss getting on the agenda.

MR. KERSHNER briefly walked through the timeline that ended with Conduent's target to issue the experience analysis report on September 1, 2018. He noted that the assumptions that the Board adopts at the June 21, 2018 meeting will be first used in the 6/30/18 valuations (for setting the fiscal year 2021 contribution rates).

E. Actuarial Communication Plan for Proposed Changes

CHAIR ERCHINGER recalled past discussion about making the assumption changes more transparent to the committee and the full Board. She said Conduent's PowerPoint presentations to the committee explain fairly well the recommended changes and why. Then the committee meetings have a record about the deliberative process on how it came to the recommendations to the full Board. She assumed that Conduent planned to articulate within the document itself how they got from the current assumptions to any recommended changes in assumptions.

MR. KERSHNER said he expected that the experience study report would have an executive summary that lists current assumptions and new proposed assumptions. The remainder of the report would contain the details of how Conduent arrived at the recommended assumptions. He added that the timeline he had just walked through was the anticipated communication or roll-out of those changes, leaving ample time for committee discussion and feedback. After that process, Conduent will be at a point where the roll-out should be fairly simple.

F. Committee Charter

CHAIR ERCHINGER stated that board liaison Stephanie Alexander was able to gather some historical records of the committee charter *[included in the meeting packet and on file at the ARMB office]*. She summarized the contents of those records for committee members. She stated that the committee charter that the committee originally voted on in 2015 needs some work and for that reason was never forwarded to the full Board for approval.

CHAIR ERCHINGER reported that Commissioner Fisher had expressed a desire to see some additional changes to the charter. He and she agreed to work together on trying to come up with charter language that they both agreed upon so they could bring a unified recommendation to the committee to vote on. The history of the back-and-forth draft versions of the charter was included in the packet, and the process got stuck at that point. She said one sticking point had to do with the committee's and the Board's roles with respect to approving actuarial assumption changes. The question was, if the statute says that the ARMB will approve assumptions that are recommended by actuaries in accordance with actuarial standards, it could be interpreted to say that the actuaries themselves were the ones setting the assumptions. The other side of the story says that the statute clearly contemplates multiple actuaries – a primary actuary and a review actuary who is reviewing the assumptions and making recommended changes. And if the Board has two actuaries recommending a different course with respect to an assumption, the Board could go to a third actuary. So, there is an implication in statute, at least in her mind, that the Board has the authority to approve the assumptions because it has various levels of actuarial review on the assumptions.

CHAIR ERCHINGER said another main issue that she recalled was still on the table from the discussions with the commissioner a couple of years ago had to do with the charter containing a request that before the committee started to work on a new valuation that it would be meeting with the actuaries and members of staff to talk about a timeline and talk about the steps, similar to what Conduent reviewed today. There was concern about the appearance that the committee felt it had the authority to require Department of Administration staff to sit down with the committee and do something. The committee does not manage that staff or have the right to tell them to appear or not appear anywhere. She thought the point was a matter of coordination, and the wording probably needs to be change to say at the direction of the commissioner of the Department of Administration whoever they deem to participate in that is their discretion. The committee does not intend to direct anybody to do anything, but it is trying to coordinate and have all the proper parties participate at the table in order to get the best input.

CHAIR ERCHINGER stated that the purpose of putting this on the agenda was to refresh everyone's memory and determine where to go from here. She added that the historical discussions took place largely in 2015 when the committee was first formulated and did not know what it was going to be doing. With two years of experience behind it, revisiting the committee charter would probably be fairly easy. She apologized for not revisiting it earlier, but the committee was focused on working on the valuations and now with the experience study. She added that Stuart Goering, the ARMB's legal counsel, had stated that a committee technically does not need a charter to operate, so long as it is not doing anything that it should not be doing. Thus, it has not been time critical for her, as chair, to put the charter on the agenda to work through the issues. However, the charter needs to be addressed, and hopefully it can all be resolved and approved within the next year or so. She urged committee members to read the history. She expected the committee would start with Mr. Goering's version, where the committee approved a charter and Mr. Goering recommended changes to it to comply with legal provisions. The goal is to eventually get a charter that everyone can agree upon.

VII. FUTURE MEETINGS

A. Calendar Review

The schedule of meetings for 2017-2018 was included in the packet.

B. Agenda Items

There were no items other than what was requested during the meeting.

C. Requests/Follow-Up

There were none.

VIII. Adjournment

The meeting adjourned at 12:14 p.m., on a motion made by Ms. Harbo and seconded by Mr. West.

Note: An outside contractor prepared the summary minutes from staff's recording of the meeting. For in-depth discussion and presentation details, please refer to the recording, staff reports, and written presentation materials on file at the ARMB office.

Confidential Office Services
Karen Pearce Brown