

Public Agenda Item #1

*Call Meeting of the ERS Board of Trustees
Audit Committee to Order*

May 20, 2020

Public Agenda Item #2

*Review and Approval of the minutes to the March 11, 2020
ERS Audit Committee Meeting - (Action)*

May 20, 2020

Questions?
Action Item

Public Agenda Item #3

Review of External Audit Reports

May 20, 2020

Tony Chavez, Director of Internal Audit

Gabriel, Roeder, Smith & Company Actuarial Audit

Tony Chavez, Director of Internal Audit

Dana Woolfrey, GRS Consulting

Mehdi Riazi, GRS Consulting

Fiscal Year 2019 Insurance Actuarial Audit



Purpose

- GFOA Best Practices – an actuarial audit is a valuable tool for monitoring the quality of actuarial services performed on behalf of the pension plan

Description

- An actuarial audit involves engaging the services of an outside actuary (reviewing actuary) to scrutinize the work of the plan's consulting actuary

Timing - Every 5 years

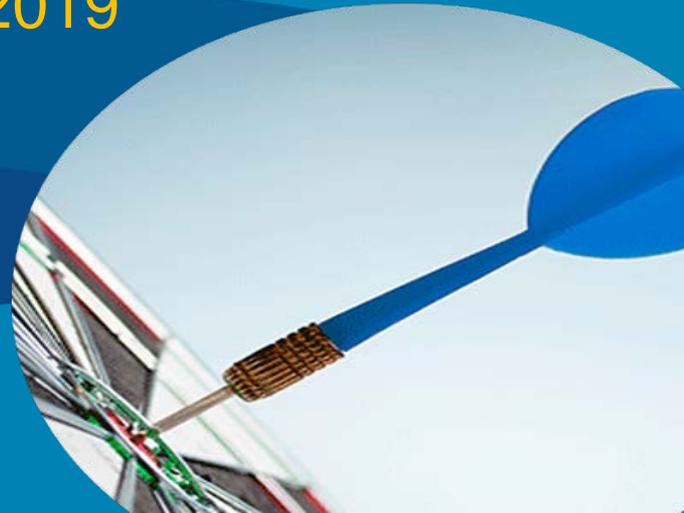
Strategic Alignment:

*Engage Stakeholders for
Informed Decision Making*



Employees Retirement System of Texas
Group Benefit Plan
Actuarial Audit of the GASB 74 Valuation for the
Measurement Period Ending August 31, 2019

May 20, 2020
Dana Woolfrey, FSA, MAAA
Mehdi Riazi, FSA, MAAA



Employees Retirement System of Texas Group Benefits Plan

Actuarial Audit of the GASB 74 Valuation for the Measurement Period Ending August, 31, 2019

Review Inputs

- Data, Assumptions, Initial Age Rated Medical and Rx Costs

YES	NO
<input checked="" type="checkbox"/>	<input type="checkbox"/>

Review Model

- Review Individual Liability Projections (Test Life Review)
- Overall actual cash flows are consistent with projected benefit payments

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Review Report

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Conclusion

- Provides a fair and reasonable assessment of the liabilities of the post-retirement healthcare plan as prescribed by the requirements of Governmental Accounting Standards Board (GASB) Statement No. 74

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Final Assessment

- All findings are minor
 - Add some detail to assumption section of report
 - Consider decrement timing in future valuations
 - Continue to review forfeiture assumptions in future valuations
- Provides a fair and reasonable assessment of the liabilities of the post-retirement healthcare plan as prescribed by the requirements of Governmental Accounting Standards Board (GASB) Statement No. 74
 - Not over or underreporting liabilities
- Clean Actuarial Audit

Purpose of the measurement

- All assessments must be made considering the purpose of the measurement:
 - Fulfilling GASB 74 requirements
 - Largely unfunded
 - Accounting Only
 - Calculations need to be in accordance with the relevant Actuarial Standards of Practice (ASOPs)

Review Inputs

Data (ASOP 23)

- Including appropriate population
 - Most active employees also participate in the ERS pension plan.
 - Active employees in higher education belong to the TRS pension plan, and ERS OPEB plan.
- Census data for individual test cases is appropriately used
- Data is correctly processed between staff file and valuation system

Review Inputs

Demographic Assumptions (ASOP 35)

- Most demographic assumptions are pension-related
 - For example, retirement, termination, mortality rates
 - Consistent with those used in ERS and TRS pension valuations, where applicable
 - Reasonable and typical approach in post-retirement healthcare valuations
- Some minor assumptions associated with terminations that are specific to OPEB valuation:
 - Do vested members leave contributions and retain eligibility or take refund?

Review Inputs

Economic Assumptions (ASOP 27)

- Discount rate based on bond index as of measurement date
- Volatile, but...
- Mandated by GASB

Review Inputs

Healthcare-Related Assumptions (ASOP 6)

- Health care trend
 - How will claims and premiums increase going forward?
 - Can health care costs continue to outpace salary growth?
- Participation and Coverage
 - Not all retirees participate
 - How many will have spouse or family coverage?
 - Which health plans will retiree select?
- Age-adjusted claims
 - Reflects the impact of age on claims costs

Review Inputs

Health Care Cost Trend Rates (ASOP 6)

- The forward looking health care trend assumptions are reasonable and consistent with the guidelines in ASOP 6
 - Initial rates are at least 7.00% for the first three years, declining to an ultimate rate of 4.50% by 2028.
 - Long-term percentage of the economy dedicated to healthcare would increase to approximately 23% by 2040 if healthcare spending grew at these rates and the US economy grew between 3.5% - 4.0% per year .
 - The 4.50% ultimate trend rate assumption includes margin above long-term GDP growth.
 - Rudd and Wisdom may want to consider extending the select period.
 - Rudd and Wisdom's use of different trend rates for different plans and fee components is a best practice.

Review Inputs

Healthcare-Related Assumptions (ASOP 6)

- Participation and coverage assumptions agree well with recent plan experience
 - 98% participation assumption for eligible retirees
 - 32% of males and 19% of females are assumed to have a spouse covered; liabilities are included for children
 - 73% of Medicare retirees are assumed to participate in the Medicare Advantage plan
- Age-utilization curves are based on plan's own experience. Reasonable for a large plan; and the rates appear reasonable.

Review Inputs

Initial Per Capita Costs (ASOP 6)

- There were no issues identified that had a material impact on the per capita cost development
 - The 2020 premiums were used as the basis of the initial costs for the fully-insured, Medicare Advantage plan
 - For the self-insured plans, the initial per capita health care costs for fiscal year 2020 were developed using claims data incurred in fiscal year 2018 and paid through November 2018
 - Claims were analyzed by plan, gender, relationship to patient and age-bracket
 - Incurral, trend, and rebate factors were applied to the FY2018 medical and pharmacy claims

Review Inputs

Initial Per Capita Costs (ASOP 6)

- Trend factors are reasonable and vary by type
 - The medical claims growth rate assumption for Hospital/Facility for FY2019 and FY2020 is 2.5% and 6.5%, respectively
 - Other Medical Expense claims growth rate in FY2019 was assumed to be 7.6% and 4.2% in FY2020
 - The prescription drug claims growth rate is 8.7% for FY2019 and 12% for FY2020 for both the HealthSelect and HealthSelect MA plans.

Review Inputs

Initial Per Capita Costs (ASOP 6)

- Revenue related to prescription drug plans
 - Formulary rebates are passed through from pharmaceutical manufacturers based on the utilization of brand drugs included on the PBMs formulary
 - For Medicare retirees who are enrolled in the Employer Group Waiver Plan (EGWP), ERS receipts include a direct CMS subsidy per individual per month, coverage gap discounts based on utilization of brand drugs, and catastrophic federal reinsurance for members whose prescription drug spend exceeds a prescribed threshold
 - The per capita prescription drug costs used in the valuation are net of revenue from manufacturer rebates and revenue related to the EGWP
 - We found the Rx rebate and revenue amounts used in the PCC development to be reasonable and in-line with data from other large health plans

Review Inputs

Initial Per Capita Costs (ASOP 6)

- Taxes
 - The Medicare Advantage medical claims were assumed to include the Health Insurer Provider (HIP) Fee, valued at \$17.66 per retiree per month.
 - The August 31, 2019 liabilities incorporated the HIP and the anticipated impact of the “Cadillac Tax”.
 - The HIP Fee and the Cadillac Tax were permanently repealed on December 20, 2019.
 - The impact of the repeal should be reflected in the August 31, 2020 valuation report.

Review Inputs

Initial Per Capita Costs (ASOP 6)

- Expenses and Fees
 - The FY2020 administrative expenses were project to be \$189.24 PMPY for medical for HealthSelect and an additional \$9.00 for prescription drugs for HealthSelect and HealthSelect Medicare Advantage.
 - The medical fee is guaranteed from BCBSTX through FY2023. The prescription drug fee is guaranteed from UnitedHealthcare/Optum through FY2022.
 - Capitation fees were also projected for FY2020 using FY2018 capitation costs and applying trend. No trend was used for FY2019 and a 3% trend was used for FY2020

Review Model

Test Life Review

- 11 actives
- 8 post-retirement (7 retiree, 1 beneficiaries)
- 3 inactives
- Test lives chosen to produce greatest assurance of overall result
 - Employee types, age, service where greatest population centers
- Rudd and Wisdom sent full test life detail
 - Transparency
 - Can ascertain rather than surmise

Review Model

Test Life Review - Results

- All test cases were within 5%
- Observed differences were explainable
 - Rounded ages vs. exact, etc.
 - Should not impact aggregate results
- Highly successful replication of test lives

Review Model

Test Life Review - Findings

- Benefits and assumptions were applied as disclosed in the report
- Some minor additional disclosures needed
 - Pertaining to termination - how many that terminate prior to retirement will come back and utilize healthcare benefits later when eligible?
 - Decrement timing

Review Model - Test Life Review

Findings, Application of forfeiture assumption

- Forfeiture assumption: If member terminates prior to retirement, will they
 - leave their contributions and receive pension and post-retirement healthcare; or
 - receive a refund of contributions?
 - Important due to dichotomy of liability: refund = none
- ERS forfeiture not a pension assumption any more
 - Using greatest economic value method
 - May continue to be most reasonable
 - Will not be maintained by pension actuary – something to stay aware of
- TRS forfeiture determined by R&W and need to disclose
- Applying forfeiture to term vesteds that left in the last year
- All reasonable, just omitted from assumption section of report

Review Model - Test Life Review

Findings, Application of decrement timing

- Rudd and Wisdom assumes probabilities for retirement, termination, death and disability apply at beginning of year
- Not consistent with application of pension assumptions in pension valuations
 - ERS all middle of year
 - TRS retirement end of year, TRS other middle of year
- Not a major finding
 - But can cause some differences in accrued liabilities and normal costs on an individual basis

Review Model

Cash Flow Checks (ASOP 6)

- 1st year expected benefit payments compared to actual benefits for 3 valuations. (\$'s in millions)

Fiscal Year Ending	2017	2018	2019
Expected benefits	\$881.7	\$882.7	\$816.4
Actual benefits	\$877.7	\$735.8	\$828.8
% difference	-0.5%	-16.6%	1.5%

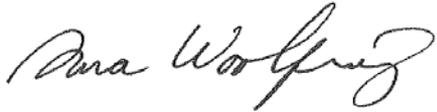
- In general, the actual benefit payments for the year following the valuation date have agreed well with the projected benefit payments from the respective OPEB valuation.
- Third party administrator and pharmacy benefit manager changes produced greater savings than expected in 2018

Conclusion

- All findings are minor
 - Add some detail to assumption section of report
 - Consider decrement timing in future valuations
 - Continue to review forfeiture assumptions in future valuations
- Provides a fair and reasonable assessment of the liabilities of the post-retirement healthcare plan as prescribed by the requirements of Governmental Accounting Standards Board (GASB) Statement No. 74
 - Not over or underreporting liabilities
- Clean Actuarial Audit

Signature Page

- This report may be provided to parties other than ERS only in its entirety and only with the permission of the Board.
- The signing actuaries are independent of the plan sponsor.
- The undersigned are Members of the American Academy of Actuaries and meet the qualification standards of the American Academy of Actuaries to render the actuarial opinions contained in this presentation.



Dana Woolfrey, FSA, EA, FCA, MAAA
Senior Consultant



Mehdi Riazzi, FSA, EA, MAAA
Senior Consultant

Questions?

Public Agenda Item #4

Review of Internal Audit Reports

May 20, 2020

Tony Chavez, Director of Internal Audit

Tressie Landry, Audit Manager

Greg Magness, Project Lead

Incentive Compensation Audit

2019 Incentive Compensation Audit



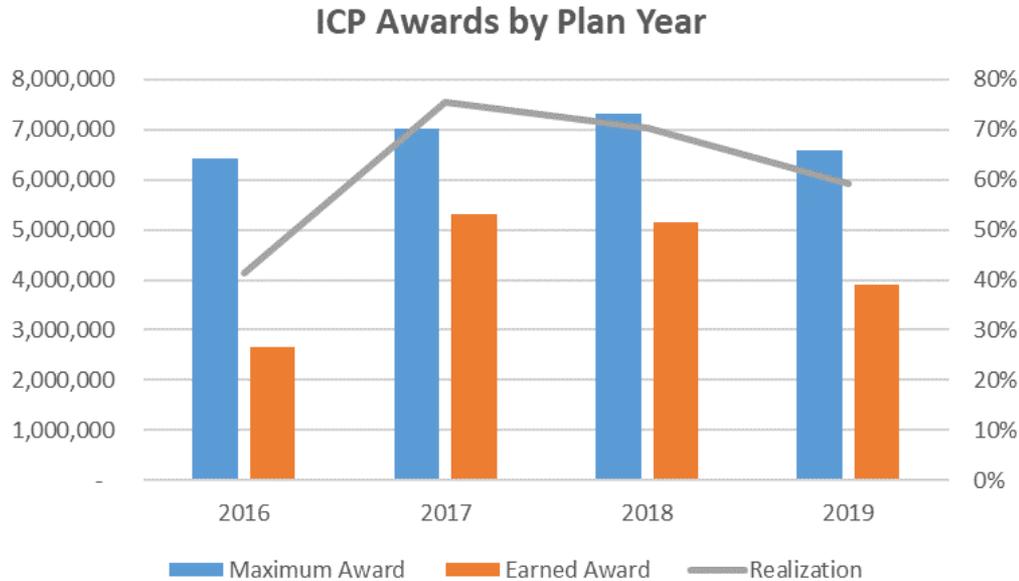
ICP Strategic Objectives

- **Strategic Alignment:** *Maintain highly skilled and knowledgeable investments staff to administer comprehensive and actuarially sound retirement programs.*
- **Program Objective:** *To provide meaningful incentive to participants who excel in implementing ERS' investment activities.*
- **Strategic Principle:** *Stewardship - Prudently manage resources.*

2019 Incentive Compensation Audit



ICP Awards - by Plan Year



Key Data Points:

- \$728,000 (10%) decrease in total maximum awards
- 57% total realization earned in PY18, down from 70% in PY18
- \$1.2m (24%) decrease in total earned awards

2019 Incentive Compensation Audit



Audit Objective and Overall Results

Determine if incentive compensation awards were in accordance with ERS' Incentive Compensation Plan.

OVERALL ASSESSMENT		SATISFACTORY
SCOPE AREA	RESULT	RATING
ICP Participation & Development	Controls are present to ensure participants are eligible and meet minimum requirements to receive an award.	Satisfactory
	Controls are present to ensure performance goals are developed in accordance with ICP guidelines.	
ICP Award Calculations	Controls are present to ensure the accuracy of recommended awards.	Satisfactory
	Controls are present to ensure recommended awards align with ICP directives.	
Follow-up on Audit Recommendations	Continue to strengthen the control framework by implementing Management Action Plans of prior audits.	Satisfactory

2019 Incentive Compensation Audit



Improvements

- Comprehensive goal crosswalk was developed and used to improve the information in the ICP Goal Memo
- Qualitative (Discretionary) Awards calculated within the ICP Database
- Change Management Log created to track adjustments to ICP Awards
- Eligibility Date added to each individual goal making clear which 1-, 3-, and/or 5-year goal the Participant is eligible

2019 Incentive Compensation Audit



Observation

- Identify and provide specific guidance for key control activities, including evidence of performance
 - Define the use of the Change Management Log, including how it will be used in tracking adjustments to ICP Awards
- Finalize the documentation of the ICP Database defining/describing the objects of the database (table, queries, forms, reports) and their associated relationships

Questions?

Public Agenda Item #5

Adjournment of the ERS Board of Trustees Audit Committee Meeting

May 20, 2020