PERFORMANCE OVERSIGHT HEARING ON THE DISTRICT OF COLUMBIA RETIREMENT BOARD FOR FISCAL YEAR 2020

Testimony of

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District of Columbia Retirement Board

Before the

Honorable Phil Mendelson, Chairman
Committee of the Whole
Council of the District of Columbia

John A. Wilson Building
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OPENING REMARKS

Good afternoon Chairman Mendelson and members of the Committee of the Whole. I am Karen Hsu, Acting Executive Director and Pension Administrator of the District of Columbia Retirement Board (DCRB or the Board). I am pleased to testify on DCRB's Fiscal Year (FY) 2020 performance. With me today are Lyle Blanchard, DCRB Trustee; Mark Spindel, Chief Investment Officer; and Thomas Vicente, Senior Consulting Actuary with Bolton, which serves as the Board's independent actuary. Before discussing the mission and priorities of DCRB, I would like to express our thanks and acknowledge the guidance and support provided by our Board of Trustees. Finally, I also want to express my appreciation to this Committee and your staff for your assistance over the past year.

OUR HISTORY AND MISSION

DCRB was created by Congress in 1979 as an independent agency of the District of Columbia Government. Our Board of Trustees collectively serve as fiduciaries with exclusive authority and discretion to manage the assets of the District of Columbia Teachers' Retirement Fund and the District of Columbia Police Officers and Fire Fighters' Retirement Fund (collectively referred to as the Fund). These assets are held in trust for the sole benefit of members of the District of Columbia Teachers' Retirement Plan and the District of Columbia Police Officers and Firefighters' Retirement Plan (referred to as the Plans), as well as their eligible survivors and beneficiaries.

The District Government is responsible for funding the benefits earned by members covered under the District Replacement Plans (the District Plans), which were adopted on July 1, 1997. Fund assets, which are pooled for investment purposes, may only be used to pay benefits and expenses necessary to administer the retirement program for the benefit of the District Plans. The District Government, as employer, is the Plan Sponsor for the District Plans. In this capacity, the District is responsible for the design of the District Plans, for certain benefits administration activities, and for paying the required employer contributions into the Fund. In addition to the employer contributions, Fund income includes employee contributions (made as a fixed percentage of pay), and investment earnings.

DCRB also serves as the third-party administrator for members' retirement benefits earned through June 30, 1997, under what are referred to as the Frozen Plans. These plans are the responsibility of the U.S. Department of the Treasury (U.S. Treasury), which reimburses DCRB for costs incurred in administering retirement services under the Frozen Plans. Any reimbursement of administrative expenses by U.S. Treasury offsets the amount required from the Fund each year.

The Board's mission includes two, overarching goals: *(1) to prudently invest and manage Fund assets,* and (2) *to administer retirement benefits by providing members with accurate and timely pension payments, as well as excellent customer service*. The projects and initiatives in progress, as well as those planned for the future, are undertaken to support this mission.

STATUS OF THE FUND AND THE PLANS

As of September 30, 2020, there were 26,979 members in the District and/or the Frozen Plans. Approximately 77 percent (20,721) of the members are now covered under the District Plans, or they are jointly funded by the District and federal governments. Although the greater portion of benefit payments are still paid by U.S. Treasury for accrued annuity benefits under the Frozen Plans, our former actuary projected that District annuity payments are expected to surpass those of the U.S. Treasury around 2031— just ten years from now.

The Board's Actuarial Valuation Report for FY 2020 indicates that the aggregate funded ratio for the District Plans was 105.1 percent (down from 105.5 percent in FY 2019). The individual Plan ratios were 92.1 percent for the Teachers' Plan and 110.8 percent for the Police Officers and Firefighters' Plan. Separately, the ratios were 110.4 percent for Police Officers and 111.7 percent for Firefighters.

For some perspective, The National Conference on Public Employee Retirement Systems—the largest trade association for public sector pension funds—recently reported that the average funded level was 75.1 percent in 2020, up from 72.4 percent in 2019.

As of September 30, 2020, the Fund was valued at $9.0 billion, an increase of approximately $511 million in total asset value over the previous twelve months. As of December 31, 2020, the Fund value had appreciated to $10.1 billion, an almost 11% gain over the quarter. The rollout of vaccine and the associated economic recovery has boosted asset markets that supports the Plans.

OUR PRIORITIES

DCRB is experiencing an intense level of transition. Although our primary goals remain unchanged from the prior year, the way we execute against them must be fundamentally different. This is not an indictment of our past, our history, or our staff; it is a reality that we must resolve the issues before us in order to move forward successfully.

As with any organization experiencing this level of change, one of the most critical activities we undertake is prioritization. Across the disciplines represented at DCRB, we need to ensure that we have a complete leadership team and Board, and stable of consultants and advisors.

Refine DCRB's organizational structure to meet changing agency responsibilities and needs.

Specific to our priority of assembling a complete leadership team, in FY 2020 we filled four key positions in the IT, Investment, and Benefits departments. Ram Murthy joined us as the IT Director in October 2019, Akiko Kawashima joined us as the Controller in October 2019, Mark Spindel joined us as the Chief Investment Officer in August 2020, and I also joined in August 2020 as the Pension Administrator. In FY 2021 we anticipate filling the Chief Financial Officer position and completing an executive search for DCRB's retiring Executive Director. The trustees have concurred that the next Executive Director should have the opportunity to select a Chief Operations Officer (COO) or Deputy Director, whose role largely will be to further improve the efficiency and effectiveness of agency operations and provide greater support to our infrastructure departments, including Procurement.

As for support within each department, we have been making great strides in filling vacancies within the various departments. We expect that a strong and robust leadership team will be a benefit not only to each department but to the agency as a whole as we work together to fulfill the mission, provide greater alignment between operational activities and strategic initiatives, and be more effective in our daily work.

Safeguard the integrity of the Fund.

Safeguarding the integrity of the fund is both the foundational and overarching goal. This is a guiding principle underlying almost every decision we make. Every dollar we spend should be the single best use of that dollar whether we save it, spend it, or invest it.

Our operations are complex and, not uniquely, they become increasingly complex over time. This is the key driver of our other top priority, which is to ensure that we have the right advisors. In FY 2021, we will engage a consultant to assist us and support us in a robust review of our operations. Specifically, these services will identify organizational areas of strength and weakness in the implementation, administration, and fiduciary oversight of the Retirement Program; compare DCRB third-party administration and other support operations, including investments and Board fiduciary oversight functions, with applicable Federal and District laws, rules, and regulations, industry best practices, and the best practices of other similarly situated governmental 401(a) defined benefit plans; and provide detailed and actionable recommendations to cure or improve any identified deficiencies. Having a strong partner will ensure that we benefit from the breadth of their perspective and experience and can move more quickly to develop and execute a plan of action.

Expand and improve benefits administration capabilities, to assure that benefits are paid to our members accurately and timely.

We must remain vigilant in our ongoing evaluation and improvement of our benefits administration capabilities and services. This certainly supports accurate and timely benefit payments but also requires that we consider improvements through the entire participant life cycle. Key goals for FY2021 are to examine and refine our service metrics and develop process maps to assist us in identifying bottlenecks and duplications of effort that impair the overall participant experience. Not only will this be a useful tool for DCRB staff, it also will support more effective collaboration and clear understanding across agencies holding data that feed into that final retirement transaction.

Prudently invest Fund assets to provide long-term, sustainable, risk-adjusted returns.

One of DCRB's major ongoing responsibilities is to prudently invest Fund assets, with the goal of earning a return that meets or exceeds our actuarial long-term net investment return assumption target of 6.5 percent. This target is intended to sustain the Fund's viability over the long-term investment horizon. From its inception, the Fund has generated returns exceeding the current 6.5 percent long-term actuarial assumed return. For FY 2020, amidst COVID-induced economic and financial market volatility, the one-year net return for FY 2020 was 5.3 percent and the strong 4th quarter gains mentioned earlier raised net calendar year 2020 returns to 10.3 percent.

In FY 2021, we will continue to routinely evaluate investment manager performance against benchmark returns, rebalance the portfolio to maintain compliance with asset allocation targets and ranges, and monitor and evaluate investment manager fees. We will continue to strengthen our important efforts to identify promising emerging diverse fund managers and engage our partners to evaluate their efforts to promote diversity and inclusion throughout their business operations. Pursuant to the Diverse Emerging Fund Managers and Reporting Requirements Amendment Act of 2020 (D.C. Law 23-161), DCRB began meeting this reporting standard in its FY 2020 Comprehensive Annual Financial Statements (CAFR).

In line with DCRB's overarching top priorities, the Board will release an RFP for Investment Consulting Services, pursuant to procurement best practices and the evolution of the marketplace for these services. We have had stable relationships in this area historically and also must ensure that these critical services remain competitive and strong.

Foster member and stakeholder trust through enhanced communications and collaborative outreach.

Building and maintaining trust is imperative to our effectiveness. It is reflected in how effectively we manage expectations, as much as in how well we fulfill them. The expectations and consequences are clear and we remain committed to doing the work required to correct our course.

We know that our participants had a high interest in meeting with us in person and the global pandemic required us to moderate how we engage. Building on our strides in FY 2020, we will continue to better leverage our website to share timely updates regarding expected and unexpected activities that may be of interest to our stakeholders throughout the year. In addition, our operational projects and service enhancements will invite participant feedback to ensure we can deliver improvements that are meaningful and effective.

CONCLUSION

Our Trustees remain engaged and committed to the agency's mission, and our staff continue to work hard to meet the needs of our members. Together, we continue to move forward in creating a comprehensive retirement system to serve the needs of Plan participants and beneficiaries over the long-term.

In closing, I would like to thank you for your support, the Board for its guidance, and the DCRB staff for their hard work. I am happy to answer any questions you may have.

This concludes my testimony.