AUDIT COMMITTEE OF THE CITY OF NEW YORK
MINUTES OF THE AUDIT COMMITTEE MEETING
WEDNESDAY, APRIL 3, 2019
AT THE OFFICE OF THE COMPTROLLER

ATTENDANCE

Chair	Michael Spitzer
Private Members	Mark Kaplan Bud Larson Bernard Rosen
Public Members	**Representing the Mayor –** John Grathwol **Representing the Comptroller –** Jacqueline Thompson
Secretary	Katrina Stauffer
Independent Auditors	**Grant Thornton LLP –** Hassan Khan, Benjamin Klein, David Platt, Michael Ryan, Cosmo Saginario **Marks Paneth LLP –** Roseanne Bowen, Hope Goldstein, Joseph Kanjamala
Others	**New York City Office of the Actuary –** Sherry Chan, Tom O'Hara, Michael Samet **Office of the New York City Comptroller's Bureau of Asset Management –** Alex Doñé, David Jeter, George Siavichay **New York City Mayor's Office of Operations –** Florim Ardolli, George Davis **New York City Comptroller's Office –** Camille Arezzo, Rosa Charles, Man Hon Cheung, Leonel Ferreira, , Michael Hecht, Susanna Tregor **New York City Office of Management & Budget –** Raymond Lee **Queens College Government and Not-for-Profit Accounting –** Jian Xiao (Teacher)

Audit Committee Meeting – April 3, 2019

I. Call to Order and Roll Call

Mr. Michael Spitzer, Chairman of the Audit Committee, called the meeting to order at 9:30 a.m.

Ms. Katrina Stauffer, the Audit Committee Secretary, took roll call; a quorum was present.

II. Motion to Accept Draft Minutes of the Audit Committee Meeting held February 27, 2019

The first agenda item was the approval of the draft minutes of the February 27, 2019 Audit Committee Meeting. Chairman Spitzer inquired if there were any comments on the draft minutes as presented. Subject to any non-substantive editorial comments submitted to the Secretary, the Committee approved the draft minutes of the February 27, 2019 Audit Committee Meeting.

III. New York City Retirement Systems Presentation: The New York City Office of the Actuary and the Office of the New York City Comptroller's Bureau of Asset Management

The next agenda item were the presentations of the New York City Retirement Systems by the New York City Office of the Actuary and the Office of the New York City Comptroller's Bureau of Asset Management.

Ms. Sherry Chan, Chief Actuary for New York City Office of the Actuary (NYCOA) introduced the other representatives of the NYCOA present.

Mr. Alex Doñé, Chief Investment Officer of the Office of the Comptroller's Bureau of Asset Management (BAM), introduced the other representatives of BAM present.

The New York City Office of the Actuary

Ms. Chan presented an overview of the NYCOA and its support of the New York City Pension Funds and Retirement Systems (NYCRS). The New York City Police Pension Funds (POLICE) and the New York City Fire Department Pension Funds (FIRE) are Pension Funds, as they are single employers. The New York City Employees' Retirement System (NYCERS), the Teachers' Retirement System of The City of New York (TRS), and the New York City Board of Education Retirement System (BERS) are Retirement Systems, as they consist of multiple employers. There are six tiers in the Systems, but only five apply to the City, with the tiers being based on when employment began and the specific Retirement System. Tier 6 started April 1, 2012, and was introduced to help manage costs. It makes up about 25 percent of the active population and in a short time has had an effect on these memberships and the normal costs and liability associated with them. There are approximately 120 special plans in total within the systems creating a more complex process. Collectively, the New York City Retirement Systems are the fourth largest public retirement system in the country.

The Actuary's job description is defined by State statute, with the main task being to calculate the pension contributions, as well as duties such as the Fiscal Notes, which is a financial analysis that accompanies a proposed change in pension plan provisions. The New York City plan provisions are written into State statute and changes go through a legislative process, with the Actuary producing financial analyses for legislators. The Fire Life Insurance Fund is a separate valuation that does not include City contributions and is funded by members. A review is conducted every three years to verify that the contributions paid by the members will support the benefits expected to be paid. State statute also dictates that every five years the Actuary looks at the actuarial assumptions and methods for deriving the contributions. The City Charter states that the New York City Comptroller and its committee must hire an independent actuary to review and audit the assumptions and methods once every four years. Auditor recommendations are taken into consideration for any changes.

The Actuary reports to each of the five boards, comprised of 50 percent elected City officials and 50 percent union representatives. The Mission Statement for the Actuary is to provide actuarial services to the City, the public, and other agencies. There are about 45 employees whose main responsibility is to calculate contributions and service the top five Retirement Systems, nine variable supplemental funds, and four closed plans under NYCRS. One division in the Actuary's Office handles the certification of the pensions payable to public servants who are at the end of their career, which includes, service retirement, disability retirement, death benefits calculated for a beneficiary, or calculated transfers from other Retirement Systems. Domestic Relations Orders are processed, as well as option factors and annuity values. A second division is responsible for everything else, and typical work products include valuation reports for each Retirement System, Governmental Accounting Standards Board (GASB) reports for pension and Other Postemployment Benefits (OPEB), and the office assists with the City's and Systems' Comprehensive Annual Financial Report, the Financial Statements, and review of notes to the financial statements.

The OPEB plan is negotiated between the unions and Office of Labor Relations, who create the plan provisions and the NYCOA then calculates the liabilities.

Regarding liability amongst different groups: The uniform groups, Police, Firefighters, Sanitation, and Correction, account for about 46 percent of liability; pedagogical, mostly teachers, is at about 32 percent; and the remainder is 22 percent. The pre-Medicare population is about a third of total liability; Medicare and Medicare Part B add up to a little over 50 percent; and the remaining is attributed to Welfare Fund contributions and the Cadillac tax. In terms of the effect on liability if the OPEB eligibility was pushed out farther, there was a very small difference, and the conclusion is that eligibility is not the key driver of cost containment.

A question and answer session took place after the presentation. Several matters were discussed including:

- The cost impact of the savings plan started early in this administration.
- It is possible there could be cost savings if the investing and administration of all plans were consolidated to eliminate redundancy; however, this may not be possible due to political pressures. No analysis has been conducted to review this possibility.
- The Medicare Part B reimbursements of $22.3 billion found are extrapolated through close evaluation.
- A cost analysis will be conducted for the pre-Medicare and Medicare Part B benefits, with the assumptions that an employee would have to retire from service to receive the benefits. The information will be provided to the Committee Secretary for distribution to the Audit Committee.
- Gains and losses are smoothed over six years.

- Capped earnings for pension contributions are as per the Internal Revenue Code 401(a)(17) pay limit and there are two 401(a)(17) limits. Government employees hired prior to July 1, 1996 were grandfathered into a higher pay limit and, for calendar year 2019, it is $415,000. Those hired after July 1, 1996 are subject to a lower cap. The current calendar year limit is $280,000.

There being no further questions, Chairman Spitzer thanked the representatives of the NYCOA for their participation in today's meeting.

Office of the New York City Comptroller's Bureau of Asset Management

Mr. Doñé presented an overview of the Bureau of Asset Management (BAM) and discussed how BAM fits into the Office of the Comptroller. The Comptroller serves as a custodian of the assets of the NYCRS, custodian of the cash assets of various agencies, and is also the Trustee of four of the five NYCRS. The Comptroller also serves as investment advisor to the five Retirement Systems, with each System making the final decisions. BAM executes these roles for the Office of the Comptroller.

The strategic asset allocation governs how the Comptroller's Office and Bureau of Asset Management invest the assets consistent with the funds' objectives to achieve a rate of return compatible with risk tolerance to meet financial obligations. The strategic allocation is reviewed every three to four years and a review is currently underway. Recommendations are expected to be completed and presented by the third or fourth quarter of this year. The goal of the strategic asset allocation study is to set the target allocations for all asset classes, target rebalancing ranges, and implementation guidelines. Not all Systems have the same strategic asset allocation. The actuarial rate, or assumed rate of return is currently seven percent for the NYCRS and diversification is a goal expressly written into each of the Systems investment policy statements primarily to reduce volatility and risk. The New York State statute contains a section commonly referred to as the 'basket clause', which informs the Systems regarding investible asset classes. The statute also allows the systems to invest up to 25 percent of their assets in "non-basket" securities. This limit is managed very closely and the asset allocation is designed with this limitation in mind.

There is a structured process of how to select public and private sector market managers that BAM recommends to boards. On the public side, manager searches are governed by the Procurement Policy Board Rules defined by New York City Charter. Consultants have a role in selecting managers for review. Teams develop recommendations jointly with the consultants to present for the boards' considerations. The private market manager selection is not governed by the statute and is conducted by BAM. New York City Pension Systems are primarily externally managed and there are currently 336 managers across all asset classes with 109 public market managers and 227 private market managers.

The largest source of funding for the Systems is investment income returns comprising 60 percent of the funding, followed by City contributions of approximately a third, and employee contributions of approximately five percent. BAM is focused on minimizing the share of New York City's budget that goes to funding the pension plan and that is accomplished by meeting or exceeding the Actuarial rate of return.

Markets and performance were reviewed for the last two quarters illustrating a V-shaped recovery from the fourth quarter of 2018 to first quarter of 2019, and examples were provided of the earnings volatility and profit warnings that impacted the fourth quarter. Positive factors led to a first quarter where the Russell 3000, BAM's index for U.S. equities, was up 14 percent.

A summary of the assets under management, or the aggregate assets, of the five Systems was provided. As of 12/31/18, TRS was the largest System, at $69.1 billion, or 37 percent of the aggregate, followed by NYCERS, POLICE, FIRE, with BERS, the smallest, at $5.8 billion. Growth assets are the largest two-thirds of the portfolio; deflation protection 23 percent; and inflation protection at 11 percent. Over the long-term, plans are doing as expected.

Private equity has been delivering over the last seven years, not only as a diversifier of assets, but as a driver of returns, and this is the first time in seven years the performance of the private equity portfolio for each of the Systems has exceeded ten percent (Net IRR). Infrastructure is a new asset class for the Systems, with returns above 14 percent (Net IRR) since inception.

A question and answer session took place after the presentation. Several matters were discussed including:

- In regard to fee arrangements for managers, when negotiating fees for the plans, BAM tries to aggregate and speak for all the Systems.
- There are over a hundred individual managers in private equity managing capital on behalf of the five Systems.
- Conclusions drawn from the sum of the last two fiscal years nets out to a recommendation for reevaluation of the strategic asset allocation and this is right time for the boards to reevaluate asset allocations.
- Private equity verification methods for pricing is conducted by the valuation policy of each manager but, generally speaking, valuation of their private investments is based on

comparable companies and comparable company analyses. All funds are audited and valuation analyses are performed to verify the marks.

- Procedures have been changed to allow for better selection of private equities and checks. Systems are being put in place that allow a look through the funds to understand all positions in underlying funds. There are also specialty consultants conducting the same analyses and providing quarterly reports to the boards.
- Information on the liquidation of private equities is not found in reports produced by BAM. However, the information is part of the due diligence process to analyze and present in investment memos to the boards.
- The boards have their own independent audit committees.
- Different factors contributing to the positive BERS market returns includes a different risk tolerance; being a smaller plan and, therefore, more concentrated; fewer managers; and timing in private markets.

There being no further questions, Chairman Spitzer thanked the representatives of BAM for their participation in today's meeting.

IV. Executive Session

There being no further business for the public session, Chairman Spitzer asked for a motion to enter into Executive Session. A motion was made to go into Executive Session for the purpose of discussing non-public financial information about The City of New York. The motion was unanimously approved.

V. Adjournment

There being no further business before the Committee, a motion was made to adjourn the April 3, 2019 Audit Committee meeting; the motion was unanimously approved.