November 29, 2021

RE: Colorado PERA Board Responses to Pension Review Subcommittee Recommendations

Members of the Pension Review Subcommittee,

The Colorado PERA Board met on November 19, 2021 and discussed the three recommendations submitted to the PERA Board from the Pension Review Subcommittee (PRS). The Colorado PERA Board's responses to the recommendations are below:

Recommendation #1 – Revise the signal light report to show green only when a 67 percent likelihood of reaching full funding by 2048 for all divisional trusts on aggregate is reached.

The PERA Board heard from staff regarding the background to the discussion that occurred at the PRS meetings and lead to this first recommendation. The Board discussed the concern voiced by members of the PRS that communicating a "Green" or "Dark Green" status when the likelihood of reaching these statuses is less than 67 percent does not give the membership and other stakeholders an accurate reflection of the potential of further contribution increases and benefit reductions triggered by the Automatic Adjustment Provision (AAP).

The current signal light report does not currently aggregate the probability information for the five pension trust funds given the differing contribution structures, demographics assumptions and funding positions of the divisions. While it is possible to develop such an aggregate view, the PERA Board feels this aggregated metric will not be instructive to our members and other stakeholders, as this metric does not align with the AAP.

Since the adoption of the signal light report in 2015, PERA has been enhancing the signal light report each year in an attempt to convey both the short and long-term probabilities of PERA achieving the stated funding goals.

In response to the Subcommittee's Recommendation #1, the Board agrees with the need to clarify the messages of the Signal Light Report and that report's relationship to annual auto-adjust probability. PERA will refine communications about both long- and short-term measures of its financial stability while preserving consistency of our Signal Light methodology.

Recommendation #2 – Shorten amortization periods used for future layers to align with the goal of reaching full funding by 2048.

The PERA Board heard from staff regarding the background of this recommendation. Gabriel, Roeder, Smith & Company (GRS) presented this recommendation to the PRS after performing an analysis of PERA's actuarial assumptions.

In 2014-2015, PERA developed its funding policy considering "best practice" guidance from a number of organizations including the American Academy of Actuaries (AAA), the Council of Consulting Actuaries (CCA), and the Government Finance Officers Association (GFOA). The funding policy is designed to determine the Actuarial Determined Contribution (ADC). As Colorado PERA's contribution rates are defined in statute, the ADC was used as a funding benchmark against the statutory funding rates. In 2015, the Board selected 30 years as the period used to amortize future layers of new unfunded liabilities generated from actuarial experience or changes in actuarial assumptions. This ADC is included in PERA's annual report. Recognizing guidance received, the policy also requires PERA to report a sensitivity analysis of different periods for amortizing future layers. The additional alternative periods included in PERA's annual report show an ADC calculated using 25, 20, and 15 years for future layers.

In 2018, the Board updated the funding policy following the passage of SB18-200 to be in alignment with the AAP. As the AAP is designed to keep PERA on a path to pay off the unfunded liability by 2048 (30 years from passage of SB18-200), the Board decided in 2018 to keep the amortization period for future layers at 30 years. Keeping the amortization periods at 30 years, acts as a stabilizing factor (to help mitigate volatility) in the calculation of the auto adjustment provision. This decision kept the Board's funding policy and how the calculation of the ADC will affect the AAP in alignment with what PERA had discussed with members of the General Assembly, PERA's membership and other stakeholders throughout the legislative process.

Shortening the periods used to amortize new layers will introduce more volatility into the ADC, which will in effect introduce more volatility into the AAP. As the AAP has a direct impact on member and employer contributions and the level of inflation protection offered to PERA's benefit recipients, the Board feels a change of this magnitude should be considered as it relates to the overall reforms enacted in 2018. As part of their on-going governance, the PERA Board is scheduled to review the current funding policy in 2023.

In response to the Subcommittee's Recommendation #2, the Board agrees to consider modifications to the periods used to amortize new layers of gains and losses in 2023 when the Board takes up their scheduled review of the Board's funding policy. This review will align with the Board's policy of reviewing the funding policy every five years.

Recommendation #3 – Have the Signal Light Report include an historical reconciliation of gains/losses by source.

The PERA Board heard from staff regarding the background of this recommendation. GRS presented this recommendation to the Pension Review Subcommittee after performing an analysis of PERA's signal light report.

In 2014, the Legislative Audit Committee recommended that PERA, "…enhance its monitoring of the Hybrid Defined Benefit Plan's funding status and projected full funding date by updating the signal light report annually and providing policymakers an assessment of the current projected funding dates of the Plan compared to the agreed-upon funding objective..."

While the signal light report does not currently show an historical reconciliation of gains/losses, PERA's annual report does include a five-year history of gains/losses. The PERA Board discussed the legislative intent of the signal light report as a measure of current projections against objectives vs. the annual report being a view into PERA financials and whether including this historical look back would add value to the signal light report when this information is available in PERA's annual report.

The Board determined it is important PERA communicate with all stakeholders as often as possible and in as many ways as possible to ensure complete transparency regarding PERA's financial outlook. As the signal light report continues to evolve, a new section may be included in the report to address the spirit of the recommendation while keeping a consistent theme in the messaging of the signal light report.

In response to the Subcommittee's Recommendation #3, the Board agrees with the need to clarify the messages of the Signal Light Report. PERA will refine communications about both long- and short-term measures of its financial stability while preserving consistency of our Signal Light methodology.

Thank you,

Ron Baker
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