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PENSION FUND COMMITTEE

Minutes of Meeting

February 20, 2014

The Sussex County Pension Fund Committee met on February 20, 2014, at 10:00 a.m. in the County Council Chambers, Georgetown, Delaware. Those in attendance included members: Gina Jennings, Todd Lawson, Karen Brewington, and Jeffrey James. Also in attendance was Michael Shone of Peirce Park Group, the County's Pension Investment Consultant. Committee members David Baker, Hugh Leahy and Lynda Messick were unable to attend.

On February 12, 2014, the Agenda for today's meeting was posted in the County's locked bulletin board located in the lobby of the County Administrative Office, as well as posted on the County's website.

Ms. Jennings called the meeting to order.

1. **Approval of Minutes**

   The minutes of the November 13, 2013 meeting were approved by consent.

2. **Actuary Assumptions for OPEB Plan**

   Ms. Jennings reviewed a chart entitled, "Sussex County Employee OPEB Plan – 2013 Experience Study", with Valuation Methods and Assumptions also included. At the November 13, 2013 Pension meeting, an Experience Study was reviewed for the Pension Plan. Today's information pertains to a similar study performed for the OPEB Plan. The information reflects the cost impact of the recommended assumption changes. If needed, Mr. Schooley, of Aon (the County's actuary), was available by conference call. The recommended assumptions include:

   a. Retirement Rates – More early retirements occur than previously thought.

      The recommended retirement assumptions include:

Decrement Age	General Rate		Dispatchers & Paramedics
	Early/Norm	30&Out	All
54	0.0%	15.0%	0.0%
55	0.0%	15.0%	100.0%
56 – 59	0.0%	8.0%	N/A
60	20.0%	8.0%	N/A
61	20.0%	40.0%	N/A
62	20.0%	30.0%	N/A
63	25.0%	30.0%	N/A
64	10.0%	10.0%	N/A
65	50.0%	25.0%	N/A
66 – 67	10.0%	10.0%	N/A
68	15.0%	10.0%	N/A
69	15.0%	100.0%	N/A
70	100.0%	N/A	N/A

Taking the above recommended changes into consideration for the retirement assumptions, an increase of $63,900 would be realized for the annual required contribution; the unfunded liability would increase $392,367.

b. Termination Rates – More employees are leaving the County prior to becoming vested. The new recommended assumptions are noted in red:

Decrement Age	Rate	
	Male	Female
20	11.6%	17.4%
25	9.2%	13.8%
30	7.2%	10.8%
35	5.6%	8.4%
40	4.4%	6.6%
45	3.6%	5.4%
50	2.4%	3.6%
55	3.4%	4.0%
60	9.6%	0.0%

Taking the two above recommended changes [Age 55: 3.4% (Male) and 4.0% (Female)] and [Age 60: 9.6% (Male) and 0.0% (Female)] into consideration for the termination assumptions, a decrease of $83,853 would be realized for the annual required contribution; the unfunded liability would decrease $955,214.

c. Investment Rate – A similar reduction – from an 8 percent to a 7.50 percent assumed rate of return – that was recently done for the Pension Plan is also recommended for the OPEB Plan.

   Taking into consideration this recommended change in the investment rate assumption, an increase of $265,007 would be realized for the annual required contribution; the unfunded liability would increase $2,966,789.

d. Future Participation – The original assumption was that 100 percent of retirees participated in the County's pension benefits; the actual number is 90 percent.

   Taking into consideration the recommended revision to the future participation rate assumption, a decrease of $183,031 would be realized for the annual required contribution; the unfunded liability would decrease $1,482,090.

e. Marital (actives only) – The County had assumed that 100 percent of the pensioners were married; the actual number is 65 percent.

   Taking into consideration the recommended change for the marital assumption, a decrease of $183,986 would be realized for the annual required contribution; the unfunded liability would decrease $1,441,990.

f. Payroll Growth – This pertains to the amortization of the County's liabilities; while this has no effect on the unfunded liability, it does increase the County's annual required contribution.

Taking into consideration all of the recommended assumptions for the OPEB Plan, the County's annual required contribution would increase by $135,255; the unfunded liability would decrease by $657,936. Previously, the County's OPEB Plan was 70.6 percent. With the recommended assumptions, the Plan would become 72.4 percent funded.

The effect of the new mortality rates (possible future required change) would result in the County's unfunded liability increasing to $12,700,879, and would lower the unfunded liability to 67.4 percent. The adoption of the recommended revisions to the above assumptions would help offset the impact of the new mortality tables.

A Motion was made by Mr. James, seconded Mr. Lawson, to make recommendation to the Sussex County Council for the adoption of the 2013 OPEB Experience Study as outlined by Ms. Jennings.

Motion Adopted: 4 Yea.

Vote by Roll Call: Mr. James, Yea; Ms. Brewington, Yea; Mr. Lawson, Yea; Ms. Jennings, Yea

3. **Investment Analysis for the Quarter Ended December 31, 2013**

Mr. Shone distributed copies of a booklet entitled, "Sussex County Investment Performance Report, December 31, 2013". The report includes information regarding the market environment for the fourth quarter of 2013, as well as quarterly and annual performances of the Pension and OPEB Plans. Although the report should be referenced for a more detailed analysis, discussion highlights include:

Mr. Shone referred members to Market Environment – 4th Quarter of 2013 (Tab 1). He reported that it had been a very good year for the stock market, as well as for the County.

The U. S. Real Gross Domestic Product grew at an annualized rate of 4.1 percent in the third quarter. Inventory accumulation drove most of the gain and reflects businesses expectations that future demand will be strong. If this does not turn out to the case, future production will likely slow, leaving inventory investment a drag on near-term economic growth.

The unemployment rate fell to 6.7 percent and has been steadily decreasing since June 2009. Although the unemployment rate has been decreasing, there has not been significant hiring. The Federal funds rate (the overnight interest rate at which banks lend money held at the Fed to other banks) has been zero since 2008; this was done with hope that the banks would, in turn, do significant lending, which did not occur.

The U. S. Stock market was up 32.6 percent and international markets were up 21 percent; both had very strong fourth quarters. Emerging markets were negative during 2013 partly due to the slowing Chinese economy. U. S. bonds (fixed income) were down 2 percent for the year and .1 percent for the quarter. High yield (junk) bonds saw positive returns; international bonds had a very negative year; inflation-sensitive assets struggled; TIPS (Treasury Inflation-Protected Securities) were down 8.6 percent for 2013; commodities were down 9.5 percent; and REITs (real estate investments) saw an increase of only 2.9 percent. U. S. equity markets did very well in the fourth quarter – all realizing 30+ percent returns, with the exception of small cap, which saw an increase of 40+ percent.

International equity markets were up 21 percent; Europe (excluding United Kingdom) – up 27.6 percent; Pacific (excluding Japan) – up 5.5 percent; United Kingdom – up 20.7 percent; and Japan – up 27.2 percent.

The U. S. dollar weakened against European currencies, but rose against most other major currencies as well as emerging market currencies. Relative to the dollar, the Euro appreciated by 4.50 percent, while the yen de-appreciated by 17.7 percent.

U. S. core fixed income returned -2 percent; this marked its first negative annual return since 1999. Due to the County's very conservative fixed income investment approach, no investments are made in Long Government Bonds, which were down 12.5 percent.

Mr. Shone directed members to the Pension Fund Performance Report (Tab II). The Pension Fund realized a fourth quarter gain of $3.55 million (net of all of investment management fees), a fourth quarter return of 5.7 percent (gross) and 5.6 percent (net – of all management fees). For 2013, a gain of $10.21 million (net) was realized, or a return of 18.1 percent (gross) and 17.7 percent (net). The fund, as of the end of the fourth quarter in 2013, had a valuation of $69.6 million, or a time weighted return of 5.7 percent. The County's investment portfolio is very well protected in the down markets; DuPont Capital realized very good returns; and the County made actuarial changes.

2013 Accomplishments

- Strong returns (improved funded status, lowered projected ARC, and increased asset value)
- Changes were made to the Wilmington Trust Investment Management Guidelines

Looking Ahead

- Consider slightly increasing equity target and/or
- Decrease return assumption (slightly)

Peirce Park Group 2013 Accomplishments

- Hired additional CFA investment analyst
- Enhanced performance report format
- Upgraded backup systems
- Extensive fixed income research

- Hired as investment consultant to Blair and Lawrence County, PA, and Caroline County, MD

Peirce Park Group Goals for 2014

- Hire additional analyst
- Alternatives research
- Website enhancement

For the quarter ending December 31, 2013, DuPont Capital Investment had an ending market value of $12,158,709, Fidelity Low Price Stock - $4,986,326, Operating Account - $3,781,046, State of Delaware Investment Pool - $41,603,867, and Wilmington Trust Bonds - $7,119,292, for a total of $69,649,239.

As of December 31, 2013, Sussex County's Pension Asset Allocation included: State of Delaware Investment Pool – 59.7 percent; Cash – 5.4 percent; Domestic Fixed income – 10.2 percent; and Domestic Equity – 24.6 percent.

For the 4th quarter of 2013, the County's pension fund was up 5.7 percent and the County ranked in the top 29 percent nationwide (out of approximately 225 public fund plans ranging in value from $10 million to tens of billions). The average plan is larger than the County's and more aggressively invested in equities. Year-to-date, the County's plan was up 18.1 percent (gross) and ranked in the 24th percentile; 2 years – up 13.9 percent (51st percentile); and 3 years – up 10.2 percent (27th percentile). The County's good performance is based on the types of equities contained in the County's portfolio. Mr. Shone again reiterated that the County is very well protected in down markets. DuPont Capital was up 33.8 percent for 2013 and 11.3 for the quarter – beating their benchmark. Since inception (September 2008), Fidelity has realized returns of 16.3 percent versus 12.4 percent. Wilmington Trust is performing exactly has hoped – very steady, buying very conservative bonds, and holding them to maturity; also buying some treasuries in January.

As a discussion point, Mr. Shone noted that the Committee may want the actuary to present information as to the impact of an additional slight reduction in the assumed rate of return; the effect of decreasing the return assumption is that the funded ratio decreases and the annual required contribution increases.

Mr. Shone referred members to the OPEB Fund Performance Report (Tab III). The OPEB Fund realized investment returns for the fourth quarter of 2013 of $1.49 million, a return of 5.5 percent (gross) and 5.5 percent (net), which slightly outperformed the benchmark by 0.25 percent (25 basis points). For 2013, the County had a $4.06 million gain (net), or a 16.3 percent return (gross), and 16.0 percent (net). The OPEB Plan has a very low expense ratio, about half of the pension fund.

2013 Accomplishments

- Very strong returns (improved funded status, lowered projected ARC and increased asset value)
- Manager changes: Hired: Harding Loevner International Equity and Terminated: BlackRock Equity Dividend and Harding Loevner Global Equity
- Changes made to the Wilmington Trust Investment Management Guidelines

Mr. Shone noted that the following items should be considered by the Committee: Consulting Plus for the OEPB Plan, and slightly increasing equity target and/or slightly lowering return assumption. It was noted that Peirce Park had put Harding Loevner (growth manager) on a watch list due to decreased performance, as well as the implementation of fund changes on January 14, 2014.

Mr. Shone stated that the ending market value of the OPEB Plan as of December 31, 2013 was $31,028,917. With a current funding status of 70.6 percent, he went on to estimate that the County was probably in the top 1 percent nationally in the funding of this liability and that the residents of Sussex County should be aware of the County's good standing. Mr. Shone will report back to the Committee regarding specific statistics to allow the County to better speak to Council as to how well positioned the County is compared to other funds. In 5 to 6 years, the County has gone from zero percent OPEB funding to 70 percent, which, according to Mr. Shone, is "unheard of". Mr. Lawson spoke to the benefit and recommended that Mr. Shone appear to Council to speak to this issue.

The County's OPEB Plan is in the 35th percentile nationally for the fourth quarter of 2013, and in the 44th percentile for the year-to-date. The OPEB Plan is even more conservatively invested than the County's Pension Plan.

Mr. Shone referred members to a separate handout entitled, "Sussex County OPEB Trust – Provisional Performance Summary as of February 14, 2014".

In January 2014, the overall stock market was down. As of February 14, the County's OPEB Plan was down half a percent and bonds were positive (.8 percent). Going into 2014, the County had been over allocated in equities (63 percent versus 60 percent); the County's OPEB fund was subsequently rebalanced on February 14. It was also noted that more than half of the recommended funds outperformed their benchmark.

Mr. Shone referred members to an article contained in Peirce Park's winter 2014 Newsletter regarding estimated returns and the conclusions used by Peirce Park. Mr. Shone inquired as to the Committee's preference to receive this newsletter by email or by hard copy. It was the consensus of the Committee to receive the newsletter by email.

Ms. Jennings thanked Mr. Shone for his presentation.

4. **Employee Pension Plan – Investment Policy Statement (IPS)**

Ms. Jennings stated that she had been working with Mr. Shone regarding revisions to the IPS, which has not been updated since 2007. With the absence of three Committee members, she requested that discussion be postponed until the May meeting. Mr. Shone then inquired as to the possibility of rescheduling the May meeting due to a prior commitment. Ms. Jennings will contact members by email regarding May's meeting and as to whether November's meeting will need to be rescheduled as well.

5. **Pension Ordinance Discussion**

Ms. Jennings referred Committee members to the revised Ordinance dealing with pension benefits for County employees. She went on to explain that the revisions were needed as a result of now requesting new employees to contribute 3 percent toward their pension benefit (after the first $6,000 of compensation).

To discuss and add explanation as to the proposed changes, a conference call was placed with Timothy Snyder, Esquire, of Young Conaway Stargatt & Taylor, L.L.P., the County's employment attorney. Mr. Snyder noted he was asked to make the necessary ordinance modifications to address the County's requirement that employees – hired after December 31, 2013 – to make a three percent pension contribution (after the first $6,000 of compensation). He noted that, consequently, this revision impacted other portions of the ordinance and required additional amendments.

The revisions to the Proposed Ordinance are included herein in their entirety, with discussion points set out in parenthesis and italics.

ORDINANCE NO.

AN ORDINANCE TO AMEND CHAPTER 26 OF THE CODE OF SUSSEX COUNTY RELATING TO PENSION BENEFITS FOR SUSSEX COUNTY EMPLOYEES.

Section 1. Amend Sussex County Code, Chapter 26, §26-3 ALLOWABLE INTERRUPTIONS by adding a new paragraph F.:

F. For a covered employee hired by Sussex County after December 31, 2013, covered employment for calculating benefits and vesting shall not include any period of uncompensated Allowable Interruption unless, within 12 months after returning from the uncompensated Allowable Interruption, such covered employee contributes from his compensation the employee contributions that such covered employee would have contributed if he was not on an uncompensated Allowable Interruption at the rate of compensation that such covered employee was earning at the commencement of the Allowable Interruption.

(*Currently, if an employee goes on an allowable interruption, the plan provides that it counts toward service. It was decided that if someone is going to be earning credit – since the plan is now a contributory plan – they should make contributions when they are in an allowable interruption.*)

Section 2. Amend Sussex County Code, Chapter 26, § 26-6 ELIGIBILITY by adding additional language to the end of paragraphs A. and E. as follows:

A. .... In no event shall a covered employee hired after December 31, 2013 receive credit for covered employment for benefit purposes for any period of employment during which the covered employee does not make the full 3% employee contribution, except for the period of the year during which the covered employee is working and earning the first $6,000 of compensation.

(*No covered employee will receive credit for any time in which they do not make the three percent contribution, except while they are earning the first $6,000.*)

E. .... To receive such credit for covered employment for time in the federal military service or federally acceptable substitute service, a

covered employee must, within the 12 months after returning from time in the federal military service or federally acceptable substitute service, contribute from his compensation the employee contributions that such covered employee would have contributed if he had not spent time in the federal military service or federally acceptable substitute service at the rate of compensation that such covered employee was earning at the commencement of the Allowable Interruption federal military service or federally acceptable substitute service.

(*Under USERRA [Uniformed Services Employment and Reemployment Rights Act], for an employee to receive such credit for the time while on federal military service, they must make contributions.)*

Section 3. Amend Sussex County Code, Chapter 26, § 26-7 COMPUTATION OF BENEFITS by adding new paragraphs E. and F. to read as follows:

E. Minimum Death Benefit. Upon the death of a covered employee, former employee or pensioner, or if a survivor's pension is payable upon such death, when such pension ceases to be payable, there shall be paid to the designated beneficiary or, in the absence of a designated beneficiary, to the estate of the covered employee, former employee or pensioner a lump sum equal to the excess, if any, of the accumulated employee contributions with interest over the aggregate of all pension payments made.

(*This provision ensures that an eligible employee or survivor will receive, at the very least, a benefit equivalent of their contributions plus interest.*)

F. Withdrawal Benefit. Upon the withdrawal from service of a covered employee who is not eligible for a service pension under Section 26-6 A, the employee's total employee contributions paid while the employee was a covered employee, with simple interest at the rate of 2% per annum, shall be paid to the covered employee.

(*When an employee leaves the service of the County and is not vested in the plan, at that point they would receive a return of their contributions, plus interest at the rate of 2 percent per annum.*)

Section 4. Amend Sussex County Code, Chapter 26, § 26-9 FUNDING by adding new paragraphs F. and G. to read as follows:

F. Employee Contributions.

(1) Covered employees hired by Sussex County after December 31, 2013, shall make employee contributions to the Fund equal to 3% of total annual compensation in excess of $6,000. In no event shall total compensation during any calendar year in excess of $6,000 be exempt from contributions. A covered employee shall at all times be 100% vested in his employee contributions.

(*This is a basic provision stating that anyone hired after December 31, 2013, shall make the 3 percent contribution and will be 100 percent vested in their contributions.*)

(2) Covered employees who were hired by Sussex County prior to January 1, 2014 and who terminate employment with Sussex County at any time and are subsequently re-employed by Sussex County after December 31, 2013 shall be required to make employee contributions to the Plan upon their re-employment except that no employee contributions shall be required from the following covered employees:

a. A covered employee who prior to such termination of employment had service with Sussex County in continuous employment for at least eight (8) years and who again becomes a covered employee within sixty (60) months of such covered employee's termination of employment; and

b. A covered employee who prior to such termination of employment did not have service with Sussex County in continuous employment for at least eight (8) years and who again becomes a covered employee within twenty-four (24) months of such covered employee's termination of employment.

(*Mr. Snyder stated that a compromise is proposed that if an employee is vested – with at least 8 years of service – and are rehired within 60 months of termination of employment, then they will be treated as a grandfathered employee. For those employees who do not have 8 years of service and are not vested when their employment terminates, they will be treated as a new employee if they are not hired within 24 months of their termination.*)

G. Employer pickup of employee contributions.

(1) The Sussex County Council, pursuant to the provisions of § 414 (h)(2) of the United States Internal Revenue Code [26 U.S.C. § 414(h)(2)], shall pick up and pay the contributions which would otherwise be payable by the employees under § 26-9 F. of this Chapter. The contributions so picked up shall be treated as employer contributions for purposes of determining the amounts of federal income taxes to withhold from the employee's compensation.

(2) Employee contributions picked up by The Sussex County Council shall be paid from the same source of funds used for the payment of compensation to an employee. A deduction shall be made from each covered employee's compensation equal to the amount of the employee's contributions picked up by the employer. This deduction, however, shall not reduce the employee's compensation for purposes of computing benefits under the retirement system pursuant to this chapter.

('Employer Pickup' is a technical term from the Internal Revenue Code and provides that employees still make the contributions; without the pickup provisions, the contributions would be considered after-tax contributions. The effect of the employer pickup is that after-tax contributions are being converted to pretax contributions. When contributions are made after-tax and the pension is paid, there must be some allocation in each pension payment between what was and was not previously taxed. Although the benefits provided with the employee contributions would be not taxable, the benefits provided with the employer contribution would be. However, if the employer picks them up, everything that is paid as pensions would be taxable because it was all pretax money.)

(3) The contributions, although designated as employee contributions, are being paid by the employer in lieu of the contributions by the employee. The employee will not be given the option of choosing to receive the contributed amounts directly instead of having them paid by the employer to the retirement system.

Discussion took place regarding two suggestions offered by Ms. Brewington:

1. Section 2. A. … add the word 'base', to read ", except for the period of the year during which the covered employee is working and earning the first $6,000 of **base** compensation"; and

2. Section 4. (2) b. change "twenty-four (24) months" to "twelve (12) months", to read "a covered employee within **twelve (12) months** of such covered employee's termination of employment"

Mr. Lawson inquired as to how the lengths of time were determined in sections 2. A. and 2. B. Mr. Snyder explained that the County's plan is not covered by ERISA (Employee Retirement Income Security Act), but 60 months is included within the Act and was the benchmark for usage with the County. Ms. Brewington stated that this is consistent with how the County handles a returning employee -- if the employee returns within that 5-year period, the employee would receive their leave accruals.

Mr. Lawson noted that interest rate language used in Section F. specifically states 2 percent and questioned if this same language should also be included in Section 3. E. Both Mr. Snyder and Ms. Brewington noted agreement that 2 percent per annum should be included in Section 3. E., to read, "… if any, of the accumulated employee contributions, with a simple interest at the rate of 2% per annum, interest over the aggregate of all pension payments made."

Mr. Snyder will make the three additional revisions and forward them later today to Ms. Brewington.

Ms. Brewington thanked Mr. Snyder for his time and assistance.

Mr. Lawson stated that Mr. Snyder's format and the three additional changes will have to be included in the original ordinance, which Mr. Moore, the County's attorney, could assist with the appropriate format. Mr. Lawson also stated the benefit of Mr. Snyder's attendance the day the proposed ordinance is presented to Council for introduction.

A Motion was made by Ms. Brewington, seconded by Mr. Lawson, that the Committee recommend to County Council the introduction of

the Proposed Pension Benefits Ordinance as presented today, with the additional 3 revisions.

Motion Adopted: 4 Yea.

Vote by Roll Call: Mr. James, Yea; Ms. Brewington, Yea; Mr. Lawson, Yea; Ms. Jennings, Yea

6. **Additional Business**

Ms. Jennings stated that Mr. Baker and Mr. Leahy were unable to attend today's meeting. Due to work conflicts, Ms. Jennings reported that Ms. Messick found it necessary to resign from the Committee; the name(s) of a recommended replacement should be emailed to Ms. Jennings. A prospective replacement would need to be a community member; could not be an employee or a pensioner; should have some type of investment background; and have no conflict of interest with the County's current investments.

Mr. James noted the County's milestone and achievement in reaching total combined Pension and OPEB assets of $100 million.

Ms. Jennings thanked everyone for their attendance.

At 11:18 a.m., a Motion was made by Mr. James, seconded by Ms. Brewington, to adjourn.

Motion Adopted: 4 Yea.

Vote by Roll Call: Mr. James, Yea; Ms. Brewington, Yea; Mr. Lawson, Yea; Ms. Jennings, Yea

Respectfully submitted,

Nancy Cordrey

Nancy J. Cordrey
Administrative Secretary