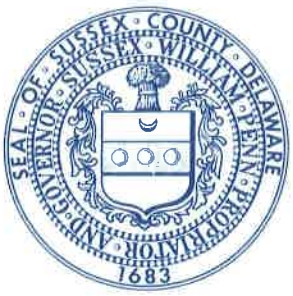
GINA A. JENNINGS, MBA, MPA
FINANCE DIRECTOR



Sussex County

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PENSION FUND COMMITTEE

Minutes of Meeting

February 26, 2015

The Sussex County Pension Fund Committee met on February 26, 2015, at 10:00 a.m. in the County Council Chambers, Georgetown, Delaware. Those in attendance included members: Gina Jennings, Todd Lawson, Jeffrey James, and David Baker. Also in attendance was Michael Shone of Peirce Park Group, the County's Pension Investment Consultant. Committee members Karen Brewington, Hugh Leahy, and Kathleen Ryan were unable to attend.

On February 18, 2015, 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 19, 2014 meeting were approved by consent.

2. **Investment Analysis for the Quarter Ended December 31, 2014**

Mr. Shone distributed copies of a booklet entitled, "Sussex County Investment Performance Report, December 31, 2014". The report includes information regarding the market environment for the fourth quarter of 2014, 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 2014 (Tab 1).

The U. S. Real Gross Domestic Product grew at 2.6 percent in the fourth quarter, which is a good sustained growth and significantly better than the global economy. Oil prices plunged during the fourth quarter. The labor market continued to strengthen and unemployment was at 5.6 percent. U. S. equities, while volatile, topped international equities once again. Core fixed income finished a strong year as intermediate and long-term bond yields continued to decline. Inflation-sensitive assets struggled among a decline in commodity prices and U. S. Dollar strength.

U. S. equities significantly outperformed international and emerging markets; U. S. Equities were up 12.6 percent year-to-date and 5.2 percent for the 4th quarter;

international equities were negative for the quarter and for the year, 3.6 and 4.9 percent respectively; emerging markets were down 2.2 percent year-to-date and 4.5 percent for the fourth quarter. U. S. bonds (fixed income) were up 1.8 percent for the quarter and 6.0 year-to-date; high yield (junk) bonds saw positive returns of 2.5 percent year-to-date and were down 1.0 percent for the quarter; and international bonds realized negative returns for both the fourth quarter (2.9%) and 4.7 percent year-to-date. Inflation-sensitive assets struggled with TIPS (Treasury Inflation-Protected Securities) seeing a zero return for the quarter and an increase of 3.6 percent year-to-date; commodities were down both for the quarter and year-to-date, 10.6 and 15.6 percent respectively; and REITs (real estate investments) saw a fourth quarter increase of 12.9 percent and 28.0 percent for the year. Although large, mid and small caps were all positive for the year and quarter, large and mid-cap significantly outperformed small cap.

Mr. Shone directed members to the Pension Fund Performance Report (Tab II).

Sussex Pension 2014 Accomplishments

- Manager searches
  - Fidelity Low-Priced Stock fund options
- Portfolio changes
  - Eliminated Fidelity Low Priced Stock fund
  - Added Vanguard Mid Cap Value Index fund
  - Added Vanguard Extended Market Index fund
- Fixed income education
- Signed new Investment Policy Statement
  - Established Delaware State Pool Target (60%), plus
  - Domestic equity target (24%)
  - Fixed Income (14%)
  - Cash (2%)

Peirce Park Group 2014 Accomplishments

- Hired additional research analyst
- Hired office administrator
- Added Thomson Reuters Datastream including MSCI data
- Equity valuation analysis
- Equity structure analysis
- Enhanced performance report format
- 3 new clients - Teamsters Local 11, Monroeville OPEB Fund and Warrington Township

Peirce Park Group Goals for 2015

- Fixed income education
- Assist clients in identifying options in challenging investment environment
- Continued technology and infrastructure upgrades
- Helping clients examine OPEB, given GASB exposure drafts

Mr. Shone reiterated that the County's OPEB Plan is one of the best funded in the country.

- Client survey
- Enhanced website

As of December 31, 2014, the ending market value of the Pension Plan was $71.6 million and realized a fourth quarter gain of $1.4 million, or a 2.1 percent return; and a 2014 gain of $5.7 million (net), or an 8.5 percent return. Mr. Shone noted that the County's returns ranked the second highest of all of Peirce Park's clients. Several manager changes occurred for the Pension Plan: terminated Fidelity Low Priced Stock, and Vanguard Extended Market Index and Vanguard Mid Cap Value were added. Strong returns were realized for 2014, which resulted in a peer group ranking in the top 3 percent nationwide and an outperformance of its benchmark by 2.2 percent. Fees were reduced from .56 percent to .52 percent resulting in a savings of approximately $28,000 per year.

Looking ahead, the County may want to consider increasing the equity target to 65 percent.

The ending market value of the Sussex County Pension Plan as of December 31, 2014 was $71,652,479, which included DuPont Capital Investment - $14,015,785, Fidelity Low Priced Stock - $0, Operating Account - $138,035, State of Delaware Investment Pool - $44,795,354, Vanguard Extended Market Index - $2,906,176, Vanguard Mid Cap Value - $2,511,992, Wilmington Trust Bonds - $7,285,137, and Wilmington Trust Short Term - $0.

As of December 31, 2014, Sussex County's Pension Asset Allocation included: State of Delaware Investment Pool – 62.5 percent; Cash – 0.2 percent; Domestic Fixed income – 10.2 percent; and Domestic Equity – 27.1 percent.

For the year, the Pension Fund realized an 8.5 percent return and ranked in the top 3 percent nationwide.

In the up markets, the County's Pension Plan performs closely with the policy index. The County's pension plan also has very good protection in the down markets.

DuPont Capital outperformed their benchmark for the last three years by 90 basis points (or nearly 1 percent); for the year, 15.5 percent versus a 13.7 percent benchmark. Although no remaining funds are currently invested in Fidelity Low Priced Stock, Mr. Shone noted – for reference – that it was up only two percent for the 4th quarter of 2014 versus their benchmarks of 9.7 and 6.1. Fidelity's replacement funds – Vanguard Extended Market Index and Vanguard Mid Cap Value – were up 6.5 percent and 7.0 percent respectively. Wilmington Trust matched their benchmark at .9 percent.

For the quarter, the State of Delaware Investment Pool was up 1.2 percent versus a benchmark of 1.7; for the year, they were up 8.0 percent versus 6.1. The State has consistently outperformed their benchmarks and no changes are recommended by Mr. Shone.

Mr. James questioned the feasibility of increasing the equity target to 65 percent. Ms. Jennings stated she was pleased with the current equity target of 60 percent and the fact that the County's plan is very well protected in the down markets. With inclusion in the State's plan, Mr. Shone noted that the County's portfolio is currently at 65 percent equities. Any rebalancing would, most likely, occur in June.

In discussion regarding County bond investments, Mr. Shone noted that Peirce Park would highly recommend Wilmington Trust (the County's bond manager) to any of their clients.

Mr. Shone referred members to the OPEB Fund Performance Report (Tab III).

2014 OPEB Accomplishments

- Implemented Peirce Park Group model portfolio
  - Eliminated Vanguard Russell 1000 Index fund, Vanguard Mid Cap Index fund, Ridgeworth Small Cap Value, and Dodge & Cox Global
- Amended Investment Policy Statement
  - Increased domestic equity target from 48 percent to 51 percent
  - Increased international target from 12 percent to 14 percent
  - Decreased bonds target from 40 percent to 34 percent
  - Increased cash target from 0 percent to 1 percent

Observations for Sussex County OPEB:

- As of December 31, 2014, the ending market value of the OPEB Plan was $30.3 million and realized a fourth quarter gain of $802,000, or a 2.8 percent return; and a 2014 gain of $1.8 million (net), or a 6.3 percent return.
- 65 percent equity target implemented
- Very strong peer group and benchmark performance
- Watch List:
  - Target – Structure
  - Thornburg – Organization

Looking ahead, Mr. Shone noted the following items for the Committee's consideration: Target – look for replacement, Thornburg – continue to monitor, and GASB exposure draft.

With a 2.8 percent return, the OPEB Plan ranked in the top 13 percent nationwide, and outperformed its policy index by 60 basis points for the quarter.

Although Thornburg performed very well for the year, Mr. Shone explained that the reason for their inclusion on the watch list was due to the fact of a significant decrease in assets. Regarding Target, he noted that while they outperformed their benchmark, they were owned by Prudential. He further explained that Prudential fired the five investment firms initially hired to manage their portfolio and then hired only one firm that was also owned by Prudential. Mr. Shone will look at possible replacements for Thornburg and Target.

Mr. Shone provided members with copies of the Pension and OPEB Investment Policy Statements and noted the benefit of reviewing these annually. The Committee will discuss both Policy Statements at their May meeting.

Mr. Baker questioned the impact of the upcoming GASB changes on the OPEB fund. At the present time, the unfunded portion – or actual liability – is included as a footnote, but will be reported on the balance sheet in the government wide financial statements; for example, if the OPEB Plan is 70 percent funded, the 30 percent unfunded portion/liability will be reflected on the balance sheet.

Ms. Jennings thanked Mr. Shone for his presentation.

3. **Potential Impact of Paramedics Switching to the State Pension Plan**

At the August 21, 2014 meeting, Ms. Jennings reported that the State of Delaware had recently passed a regulation that would allow County Paramedics to participate in the State's Pension Plan (not the OPEB). She had reported that an analysis was currently being performed by the State as to the cost to the County; the County would then have its actuary review and make comment as to the impact to the County. Participation would be voluntary, but all County paramedics would have to elect to participate.

Committee members were presented with letters from both the State's and County's actuaries noting their analysis, as well as a spreadsheet prepared by Ms. Jennings summarizing the proposed changes and impact.

Sussex County Paramedics Possible Buy-In to State Pension Plan

	With Medics	All Buy-In	10-Year Buy	5-Year Buy In	No Buy-In
Actuarial Liability	$ 72,658,831	$ 62,119,572	$ 66,360,987	$ 69,286,633	$ 72,658,831
Cost to Buy-In		$ 16,930,051	$ 9,585,622	$ 5,063,749	
Assets	$ 64,419,205	$ 47,489,154	$ 54,833,583	$ 59,355,456	$ 64,419,205
Unfunded Liability	$(8,239,626)	$(14,630,418)	$(11,527,404)	$(9,931,177)	$(8,239,626)
Annual Req'd County Contribution	13.50%	17.76%	16.11%	15.26%	14.18%
Annual Req'd Employee Contribution	0-3%	7%	7%	7%	7%

Some other considerations:

1. County buys in at a fully funded rate, but the State still recoups their unfunded liability in the Annual Required Contribution.
2. The State tells us what the County pays. The County is no longer part of the investment process.
3. OPEB is not included.

Current Scenario – "With Medics"

Actuarial Liability	$72,658,831
Cost to Buy-In	
Assets	$64,419,205
Unfunded Liability	$(8,239,626)
Req'd Annual County Contribution	13.50% of gross payroll
Req'd Employee Contribution	0 to 3 percent (3% for those hired after January 2013)

Option 1 – All Buy-In

Actuarial Liability	$62,119,572
Cost to Buy-In	$16,930,051
Assets	$47,489,154
Unfunded Liability	$(14,630,418)

Req'd Annual County Contribution	17.76% of gross payroll
Req'd Employee Contribution	7%

The State's Plan offers higher replacement income and disability benefits than the County, which results in a higher liability and pay-in for the County. The County is currently 90 percent funded, but with Option 1 this would decrease to 76 percent. Not only would the County's annual required contribution increase, but the employee's contribution would increase to 7 percent. Currently, the contribution for employees is zero to 3 percent depending on their date of hire. Of the almost $17,000,000 to buy-in, one-third of the cost would come from the medics themselves, or $52,000 per medic ($5.6 million total), which is not favorable to the medics; the County would pay the remaining two-thirds, or $11.3 million.

Option 2 – 10-year Buy-In

Actuarial Liability	$66,360,987
Cost to Buy-In	$ 9,585,622
Assets	$54,833,583
Unfunded Liability	$(11,527,404)
Req'd Annual County Contribution	16.11% of gross payroll
Req'd Employee Contribution	7%

Again, one-third of the cost to buy-in, or $9.6 million, would come from the medics, and the plan would go from 90 percent funded to 83 percent.

Option 3 – 5 year-Buy-In

Actuarial Liability	$69,286,633
Cost to Buy-In	$ 5,063,749
Assets	$59,355,456
Unfunded Liability	$(9,931,177)
Req'd Annual County Contribution	15.26 of gross payroll
Req'd Employee Contribution	7%

Option 4 – No Buy In

Actuarial Liability	$72,658,831
Cost to Buy-In	
Assets	$64,419,205
Unfunded Liability	$(8,239,626)
Req'd Annual County Contribution	14.18% of payroll
Req'd Employee Contribution	7%

The 14.18 percent required annual County contribution is determined by the State, and the County would have no control regarding the State's investment policies. If the State's pension fund decreases, or is not entirely funded, the County would be required to pay the extra cost.

Ms. Jennings stated that it is the County's ultimate decision as to what changes, if any, are implemented. It was the consensus of the Committee that the proposed changes would be detrimental not only to the County, but to the medics as well. Ms. Jennings expressed concern in County personnel being part of a pension plan that is managed by

someone else. She will release information to the medics and will explain that the numbers are not favorable to both employer and employee – from a financial standpoint – to move forward.

4. **Additional Business**

None.

5. **Adjourn**

At 10:56 a.m., a Motion was made by Mr. James, seconded by Mr. Lawson, to adjourn.

Motion Adopted:	4 Yea.
Vote by Roll Call:	Mr. James, Yea; Mr. Lawson, Yea; Mr. Baker, Yea; Ms. Jennings, Yea

Respectfully submitted,

Nancy Cordrey

Nancy J. Cordrey
Administrative Secretary