

ANNUAL REPORT – 2012

The Kent County Pension Review Committee's Annual Report to Kent County Levy Court - February 21, 2013



Structure and Purpose

The Kent County Pension Review Committee was established by Kent County Levy Court to advise the body on "the various aspects of the Kent County Employee Pension Fund." The Committee is composed of three knowledgeable members of the community appointed by Levy Court – including David Craik, Tom Leary, and Ronald D. Smith (appointed effective 02/28/12), the Kent County Finance Director Susan Durham, and the Kent County Comptroller Georgette Williams, who serves as an *ex officio* member. The Kent County Employee Council representative, J. Kelly Crumpley, passed away suddenly on 01/14/13. Levy Court appointed Kristopher Connelly as the new employee representative on 02/12/13. The Committee meets regularly on a quarterly basis to review the pension fund performance report and more often as needed to conduct additional business such as new fund manager interviews.

The Committee is also responsible for reviewing investment performance of the Retiree Benefits program (OPEB) invested with the State of Delaware Local Government OPEB Pool through the State Pension Office.

Kent County Levy Court serves as the Board of Trustees and is the fiduciary for both plans.

Investment Strategy

Per the Pension Investment Policy adopted by Kent County Levy Court, the Committee is committed to maintaining an average 60/40 asset investment ratio between equities (stocks) and fixed income (bonds).

The portfolio is structured to maintain an average balance of 25% for large capitalized growth stocks, 25% for large capitalized value stocks, 10% for international non-US growth stocks, and 40% for fixed income. Rebalancing can occur as necessary, but historically happens once per year upon transfer of the County's annual contribution.

During 2012, the Committee continued to closely monitor the erratic performance of the international equity fund manager and on a quarterly basis reviewed the performance of the State of Delaware pension fund to help it determine the best time to transfer management of the retirement fund assets to the State Pension Office. Levy Court considered the asset transfer issue in late 2010 and again in early 2011, but opted to continue to wait until consistent growth of the equity market appeared certain and invested principal was fully recovered. The Committee reviewed an internal report on 11/15/12 indicating that the plan's performance was comparable to that of the State managed pension and OPEB funds. The Committee reached consensus that the asset transfer proposal should be shelved, since its ongoing unsettled status has impacted long range planning. It was agreed that a formal recommendation on the matter would be coupled with an international equities fund manager solution in early 2013.

Investment Managers

The Pension Fund's investment managers include INTECH (large cap growth) effective November 30, 2003; Wedge Capital Management (large cap value) effective September 30, 2004; McKinley Capital Management (international growth) effective November 30, 2007; and Amalgamated Bank (core bond) effective May 1, 2008. Segal Rogerscasey LLC serves as pension consultant responsible for independently evaluating investment manager performance. Wells Fargo Retirement Services performs pension custodian services including distribution of monthly pension checks/direct deposits.

Fund Performance

The pension fund's value increased to \$26.6 million by the end of 2012, up from \$24.4 million the previous year. This figure includes a \$1,478,654 annual contribution recommended by pension fund actuary, Grant Thornton, LLC, in its report dated February 23, 2012. Over the one year period the total Fund value increased +11.29% while the comparative policy index (50% S&P 500/40% Lehman Brothers Amalgamated/10% MSCI

EAFE) grew +11.50% over the same time period. For the year, INTECH was behind the Russell 1000 growth Index (+15.26%) with a return of +14.80% in the large cap growth segment. Wedge Capital returned +15.14% in the large cap value segment, which underperformed the Russell 1000 Value Index (+17.51%). Amalgamated Bank investments increased a notable +4.62% for the year while policy index Barclays Capital Aggregate returned +4.21% for the same time period. International Large Cap Core Equity Manager McKinley Capital Management continued to struggle with a gain of +14.98% compared to the MSCI EAFE index which was up +17.32 for the year.

The retiree benefits fund managed by the State Pension Office experienced good gains during the year growing +11.8% through its commingled investments compared to +11.4% for the policy benchmark for a year end market value of \$11,028,790.10, which included a net \$91,161.27 contribution (\$661,025 less \$569,863.73 for estimated retiree benefit costs in FY2012). At year's end, 89 retirees received County health benefits, 18 dependents were covered, and 12 retirees waived coverage.

Actuarial Valuations

The annual valuation was completed as of January 1, 2012 by Grant Thornton, LLC and recommended a contribution of \$1,478,654 for FY2013. The figure was \$48,840 lower than the previous \$1,527,494 and was attributed to the improving stock market, static pay rates, and fewer employees. The next pension plan actuarial valuation is underway as of January 1, 2013. The biennial OPEB valuation was completed as of January 1, 2011 and recommended an annual contribution of \$661,025 for FY2012 & FY2013. The figure was \$30,049 higher than the previous \$630,976. An OPEB valuation is also underway as of January 1, 2013.

Plan Changes

No plan amendments were adopted in 2012. An application for an IRS Governmental Plan Determination Letter submitted by the January 31, 2011 deadline, however, did generate a response by year's end. On December 14, 2012, the IRS acknowledged the determination letter request as a "Late amender for GUST" and offered to issue a favorable tax-exempt determination if the plan would enter into a Closing Agreement Program, pay a \$10,500 sanction, and formally amend the ordinance as proposed by Pension Attorney Carol Calhoun as part of the application submission. These amendments would incorporate language related to various federal pension provisions adopted since 1974.

Fund Expenses

Pension and fee payments are drawn from the fixed income (bond) segment and transferred to Wells Fargo, on a monthly basis. For 2012, pension payments totaled \$1,898,946.98 with a total of 173 recipients at year's end. The annual fee for pension consultant Segal Rogerscasey was \$26,000, although the current agreement expired July 1, 2006. The fund custodian fee paid to Wells Fargo Retirement Services was \$14,723.29 for processing checks, reports, and trades. There were no legal fees paid to Calhoun Law Group P.A. in 2012. Actuary expenses totaling \$18,708 were paid to Grant Thornton for the valuation, various studies, and pension benefit calculations. In 2012, fund manager fees were \$37,811.93 (INTECH-0.52%), \$36,836.29 (Wedge-0.55%), \$24,360.11 (McKinley-1.00%), and \$10,604.86 (Amalgamated-0.12%). Except for Wedge, which is paid directly, such fees are assessed from investment proceeds.

Comments and Recommendations

In spite of the national election and looming fiscal cliff, the equity markets continued in an upward direction in 2012 and the fund benefitted from that double digit growth. Two of the equity managers continued to parallel the indices, and the fixed income manager remains a growth leader in a difficult sector. Overall, the pension fund's performance was "very solid" in 2012, and the Committee is confident that fund value will continue to grow as the economy improves. The Committee is saddened by the loss of employee member Kelly Crumpley and will miss his intellect and passion for the County's pension program. Finally, the Committee recommends prompt consideration of a new international equity fund manager and believes a new manager will provide the portfolio with a desired global investment exposure without replicating the underwhelming performance of the current manager.