# ANNUAL REPORT – 2016

## The Kent County Pension Review Committee's Annual Report to Kent County Levy Court - February 16, 2017

### Purpose and Structure

The Kent County Pension Review Committee was established in 1993 by Kent County Levy Court "to regularly review the investment performance of the Kent County Employee's Pension Fund, the Retiree Benefits Trust Fund, and other such funds as directed by Levy Court. The Committee oversees fund valuation processes, ensures compliance with applicable pension, OPEB, or other such funds rules and regulations, directs studies and fund manager searches, as necessary, and as a result makes prudent recommendations and reports to the Levy Court of Kent County regarding plan amendments, investment policies, investment strategies, professional fund manager(s) or trustee(s), investment advisor(s), etc."

The Committee structure was amended by Levy Court on December 13, 2016 to include four (4) citizens from the community with pension, investment, legal, or financial experience, the Kent County Administrator (by virtue of position), the Kent County Director of Finance (by virtue of position), and one Kent County employee representative nominated by the Kent County Employee Council or similar successor group. The current membership includes Chairman David Craik, citizen member Timothy R. Horne, citizen member Christopher S. Smith, and citizen member Ronald D. Smith, Kent County Administrator Michael J. Petit de Mange, Kent County Finance Director Susan Durham, and Kent County Employee Council representative Kristopher Connelly. The Committee meets regularly on a quarterly basis to review the pension fund and OPEB performance reports and more often as needed to conduct additional business such as new fund manager interviews.

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 on March 11, 2014, the portfolio is structured to maintain an average balance of 22.5% for large capitalized US growth stocks, 22.5% for large capitalized US value stocks, 10% for international non-US growth stocks, 10% for balanced risk (GTAA), and 35% for fixed income. Rebalancing can occur as needed, but was unnecessary in 2016 as the Committee directed investment of the County's entire annual contribution into the fixed income portfolio to replace regular pension payment/expense withdrawals.

### Investment Managers

The Pension Fund's investment managers include INTECH (large cap growth) effective December 1, 2003; Wedge Capital Management (large cap value) effective October 1, 2004; Rogerscasey Target Solutions (international growth) effective June 1, 2013; Invesco (balanced risk/Global Tactical Asset Allocation) effective May 1, 2014; and RCTS Core Fixed Income (fixed income) effective January 1, 2015. Segal Marco Advisors 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 $1.8 million by the end of 2016 to $34.7 million, up from $32.9 million the previous year. This figure includes a $1,821,962 annual contribution as recommended by former pension fund actuary, Grant Thornton, LLC, in its report dated March 10, 2015. Over the one year period the total Fund value increased +7.34% while the comparative policy index (S&P 500, Barclays U.S. Aggregate, MSCI EAFE) grew +6.51% over the same time period. For the year, INTECH was behind the Russell 1000 growth Index (+5.90%) with a return of +7.08% in the large cap growth segment. Wedge Capital returned +13.81% in the large cap value segment, which underperformed the Russell 1000 Value Index (+17.34%). RCTS Core Fixed Income investments earned +3.03% compared to the Bloomberg Barclays U.S. Aggregate policy index (+2.65%) for the fixed income/bond segment. RCTS Target Solutions LLC (International Large Cap Core

Equity) was ahead of the index with a return of +2.13%, compared to the MSCI EAFE (Net) index which returned +1.00% for the year. Invesco (Balanced Risk/Global Tactical Asset Allocation) surged with a +12.62% return which significantly outperformed the MSCI World/40% Bloomberg Barclays U.S. Aggregate Index (+6.09%).

The retiree benefits fund managed by the State of Delaware Pension Office was even for the year with a +6.9% return through its commingled investments compared to +6.9% for the policy benchmark for a year end market value of $14,658,370.86, up considerably from $13.5 million in 2015, and included a net +$2,536 annual contribution ($616,016 less $613,480 for estimated retiree benefit costs in FY2016). At year's end, 99 retirees received County health benefits, 22 dependents were covered, and 16 retirees waived coverage.

## Actuarial Valuations

The annual pension valuation was completed as of January 1, 2016 by new actuary The Nyhart Company, LLC and recommended a contribution of $2,166,460 for Fiscal Year 2017. Kent County typically makes a partial contribution at the mid-point and near the end of the ensuing fiscal year. The figure was $344,498 higher than the previous $1,821,962 actuarial recommended contribution. The next pension plan actuarial valuation is underway as of January 1, 2017.

The biennial OPEB valuation was completed as of January 1, 2015 and recommended an annual contribution of $785,111 for FY2016 & FY2017. The figure was $169,095 higher than the previous $616,016. Nyhart has subsequently completed a preliminary GASB 74/75 OPEB valuation as of July 1, 2016 and recommends a contribution of $1,218,059 for FY2016/17 and $1,248,883 for FY17/18. An interest rate study is pending completion and the assumption recommendation could impact the final actuarially determined contribution.

## Plan Changes

While no formal pension or retiree benefits plan (ordinance) amendments were adopted in 2016, Levy Court did consider the potential impact of Governmental Accounting Standards Board Rules #74 & #75 and approved a Committee recommendation on July 12, 2016 to change the Retiree Benefits (OPEB) program fiscal/plan year to July 1 – June 30 effective July 1, 2016, and incorporate actuarial assumptions based upon the RP2000 Combined Healthy Mortality Table with mortality improvement projected to 2016 with Scale AA, the actuary recommended health care cost trends, and the Entry Age Normal level percentage of salary cost method. For comparison purposes, the funding policy changes resulted in a net $6.2 million unfunded OPEB liability and 71.6% funded ratio versus a $1.2 million OPEB liability and 92% ratio under the former assumptions as of January 1, 2015. In addition, the Committee requested the actuary complete an OPEB Interest Rate Study as well as a Pension Plan Experience Study – both of which are currently underway.

## Fund Expenses

Pension and fee payments are drawn from the fixed income (bond) segment and transferred to Wells Fargo, on a monthly basis. For 2016, pension payments totaled $2,300,696.29 with a total of 199 recipients at year's end. The annual fee for pension consultant Segal Rogerscasey was $26,000. The fund custodian fee paid to Wells Fargo Retirement Services was $14,845.89 for processing checks, reports, and trades. Actuary expenses totaling $18,700.00 were paid to Nyhart for the valuations, various studies, and pension benefit calculations. In 2016, fund manager fees were $43,326.76 (INTECH-52bps), $43,410.17 (Wedge-55bps), $15,564.76 (Invesco-45bps), and no direct fees for the two RCTS funds. Except for Wedge, which is paid directly, such fees are assessed from investment proceeds. Retiree benefits fund (OPEB) custodian fee and investment manager/advisory fee expenses drawn from investment proceeds totaled $6,633.46 in 2016

## Comments and Recommendations

Global equity markets, led by the United States, saw strong positive returns for 2016. This came on the back of a rise in global populism, as witnessed by the Brexit vote and Donald Trump's victory in the U.S. presidential election. The US bond market started the year strong, as interest rates remained low, and finished the year in moderate positive territory as 10-year bond rates rose. Overall, the County's Pension fund gained over 7% for the year. The Committee believes the current investment structure has well positioned the portfolio for market correction, but recommends careful consideration of proposed actuarial assumption adjustments and a thorough review of the financial implications of current benefit plan designs for long term program sustainability.