

Minutes

DeKalb County Pension Board

March 15, 2018

The DeKalb County Pension Board held a meeting on March 15, 2018 in the Board of Commissioners Conference Room. The following members were present: James Hendrix, David Littlefield, Dianne McNabb, Robert Robertson, Benita Ransom, Cornelius Yarbro, and Edmund Wall. Others present: Rocky Joyner of Segal Consulting; Patricia Keesler of Benefits Law Group; Todd Carabasi, Weston Lewis, and Brad Penter of Callan Associates; and Kenny Pinkerton.

Ed Wall opened the meeting to order. Robert Robertson requested discussion of the January 11, 2018 minutes. Mr. Robertson pointed out a typo in his name and Kenny Pinkerton indicated the correction was already made for the final report. Mr. Robertson also requested clarity around a retired attendee at the meeting who indicated he had not received a benefit increase in 17 years. Members agreed that for some retirees that may be possible. David Littlefield motioned, James Hendrix seconded, and the Board approved the January 11, 2018 minutes.

Robert Robertson motioned, Eric Hendrix seconded, and the Board approved payment of the following invoices.

Vendor	Service	Period	Amount
Advent Capital Management	Investment Management	4Q 2017	\$74,663.12
Denver Investments	Investment Management	4Q 2017	76,481.92
Earnest Partners	Investment Management	4Q 2017	130,665.94
The Edgar Lomax Company	Investment Management	4Q 2017	43,139.08
Frontier Capital Management	Investment Management	4Q 2017	153,852.31
Gabelli Asset Management	Investment Management	4Q 2017	230,087.00
Income Research + Mgt.	Investment Management	4Q 2017	41,079.04
Ivy Asset Management	Investment Management	4Q 2017	56,954.41
Jennison Associates	Investment Management	4Q 2017	163,982.75
Loomis Sayles	Investment Management	4Q 2017	58,937.05
Subtotal			\$1,029,842.62
Todd M. Antin, MD	Disability Examination	January 2018	\$1,940.00
ASM Consulting	Website Maintenance	January 2018	75.00
Benefits Law Group	Legal Consulting	January 2018	3,952.50
Benefits Law Group	Legal Consulting	February 2018	1,657.50
DeKalb County Finance Dept.	Pension Administration	4Q 2017	104,655.62
Erich Randolph, MD	Disability Examination	February 2018	750.00
Segal Consulting	Consulting	Dec 2017 – Feb	8,375.00
State Street	Custodial Supervision	4Q 2017	41,571.04
Subtotal			\$162,976.66
Total			\$1,192,819.28

Weston Lewis of Callan LLC summarized the investment results for 2017. Mr. Lewis introduced the “periodic chart,” a colorful single-sheet summary of the historical investment returns to highlight the importance of diversification. Given the positive returns the last two years, Mr. Lewis indicated that 2016 and 2017 remain more of an anomaly of investment results vs. what has occurred the first quarter of 2018. Growth stocks provided the highest return with large-cap investments performing better than small-cap investments. Investment in higher risk holdings performed well as did international emerging market investments. As a measure of volatility there were more risk records set during the year than return records. Volatility is measured by the volatility index which describes how volatile the market is expected to be over the near term. Since 1993, there have been only 9 trading days where the volatility index reported a factor of 10, a very low trading volume. During 2017 there were 54 trading days with volatility rating below 10, indicating record volatility. There were only 8 trading days during the year where the volatility index was up more than 1% or down more than 1%, including no days during the fourth quarter. Another record was that the S&P Index was up every month during the year, a first in nearly 100 years of market trading.

The total fund balance is approximately \$1.4 billion at the end of 2017. In terms of asset classes, the fund is about 4.6% above the weighting target for domestic equities and underweight in fixed income and international equity, which suggests that the fund is close to taking action on rebalancing and will be watched closely. Compared to other public funded plans, the domestic equity is in the top 1%, a big positive for the fund the last couple of years.

Although it was a difficult quarter for the active managers, the manager effect for the year proved to be positive by contributing 1.28% to the fund performance. Mr. Wall noted that the fund’s management fees cost approximately 35 to 40 basis points per year, and thereby having an active managed fund is contributing to the performance vs. an indexed fund strategy. The manager effect over the past three years and five years was not as effective, adding to the cost of plan. If the managed fund strategy continues to add value, the manager effect will turn positive over time.

Compared to the Callan Public Fund database, the 18.87% return ranked in the top 5% for the year, and the fund is in the top one-third for the past five years. The Callan Public Fund database consists of 300 large public funds with more than \$100 million in assets. Comparing the public funds in the database as if they had the same asset allocation as DeKalb’s fund over the year reveals that in 2017 the fund would be in the top 14%, with the three year and five year results being closer to the median return. There are times when bias in the portfolio create a tailwind and times when bias create a headwind.

There was a small detraction in the large cap growth sector in the fourth quarter, primarily due to the transition of Montag & Caldwell to Loomis Sayles. For the full year however, the large cap growth exceeded the benchmark, with Edgar Lomax continuing to perform very well. The small cap sector performed well, led by Earnest Partners. Frontier lagged behind the benchmark by almost five percent due to their quality strategy of buying at more reasonable prices. T. Rowe Price performed well in the international sector, as did the fixed income holdings. Overall, the manager performance results are in line with expectations. Mr. Wall inquired about Ivy Investments, which is the former Waddell & Reed advisor and

Marathon, which replaced GMO. There are places for improvement, including Southeastern who has a large cash position waiting for opportunities to fit their valuation criteria. Mr. Wall asked about the possibility of placement agent fees with any of the managers, and there is no knowledge of this activity occurring, which is becoming rare.

Mr. Wall summarized the average fund returns as 18.87% in 2017, 8.0% for the last three years, 10.88% the last five years, and 7.29% for ten years. These results do not include fees, which average around 35 basis points.

Brad Penter of Callan LLC provided an analysis of Callan's annual Capital Market Projections, outlining market projections by major asset classes for the next ten years. The summary forecast is designed to help clients develop a long-term strategy and position their portfolio accordingly. The projections include various factors defining economic growth such as interest rates, GDP, inflation, etc. and are developed using a set of asset mixes to achieve a diversified investment strategy. There are no major changes in the summary from last year. The projections could also be tailored to a client's current portfolio mix. Mr. Wall noted that the projected models include alternative investments, which are not currently part of our portfolio. Mr. Penter indicated that the Board could shift the portfolio with more equities in lieu of the model's alternative asset mix. Mr. Wall also noted that highest projected return was only 6.5%, which lends credence to the Board's decision in January to lower the discount rate to 6.5%. Mr. Lewis reiterated the need to diversify the portfolio, because the typical projections are over on some asset classes and under on other asset classes.

Robert Robertson motioned, Eric Hendrix seconded, and the Board approved \$10 million funding (\$6 million from Southeastern, \$2.5 million from Jennison, \$1 million from Frontier, and \$0.5 million from Earnest Partners) for benefit payments in April-May 2018.

Todd Carabasi presented a summary of moving the T. Rowe Price International Core Fund to a commingled arrangement. This transaction has been discussed several times in past years but never took ground because the Georgia legislature did not permit commingled funding vehicles. The legislature recently passed a law allowing commingled funding and removed the OCC requirement, so it is being considered again. The main catalyst driving the change to a commingled vehicle is a reduction in management fees from 75 basis points to 55 basis points that could save the fund approximately \$276,000 per year. Another advantage is there is no need to set up separate custodial accounts in each country where investments are held. The same investment strategy is being employed in the commingled arrangement as the current core fund, so performance should remain very close or perhaps a little better. There is no fund ticker or public disclosure for the commingled fund. It is regulated and overseen by the state of Maryland, not the SEC. The migration includes an in-kind transfer from the current core fund with some operational risk being very small. A legal review representing counsel opinion is required for approval. The net asset value is expected to be valued daily and is net of the fee. Ed Wall questioned the regulation by the state of Maryland. Mr. Carabasi responded by assuring Mr. Wall that the fund is less standardized but is still regulated and requires a trustee, which is State Street. Dianne McNabb inquired about the cost savings being from state regulation vs. the SEC. Mr. Carabasi responded that there is an economy of scale utilizing a \$100 million minimum with less cost of not having to

register with the SEC. Mr. Wall brought up the possibility of a large withdrawal by another participating member which could affect performance. Mr. Carabasi responded that there could be some risk with a large outflow of funds but the overall investment strategy mirrors that of the current core fund with large holdings still in place due to the \$100 million minimum. Ms. McNabb asked Callan for more information about some of the other investors. David Littlefield motioned, Eric Hendrix seconded, and the Board approved the transition of the T. Rowe Price International Core Fund to a commingled investment vehicle.

Ed Wall highlighted a discussion of the proposed 2018 budget. Total revenue is expected to be \$74.6 million including county contributions of \$48.2 million, and employee contributions of \$25.1 million. Expenses include \$143 million for benefit payments, approximately one-half of the contribution amounts. A discussion ensued about the \$1.1 million loan repayment with Dianne McNabb indicating that the county is close to finalizing the remaining amount, which is estimated to be \$3 million. Eric Hendrix motioned, Robert Robertson seconded, and the Board approved the 2018 budget.

Rocky Joyner of Segal Consulting provided a summary of the April 1, 2017 valuation. Mr. Joyner reiterated the importance of diversification in the fund to return the best possible gain during the positive years and minimizing risk in the down years. Mr. Joyner indicated that Segal is starting the process of determining the January 1, 2018 valuation and targets completion by late summer. The January 1, 2018 valuation could potentially supersede the 2019 budget results reflected in the April 1, 2017 valuation since it will be more current and will include the strong investment results for all of 2017. The April 1, 2017 report displays a contribution amount of 21.7% of payroll for the 2019 plan year, slightly higher than anticipated due mostly to salary increases exceeding 4% in 2016 versus an assumed rate of 2.75%. The fixed amortization period is down to 26 years. Once the period is down to less than 15 years, there is some flexibility in the county contribution amount if it is needed. The strong market gains in 2017 are being smoothed over ten years, but this is also the last year reflecting 2008, thus creating approximately \$59 million in deferred investment gains that will be recognized in future years. The plan is also up for an experience study in 2018, due every five years. Mr. Joyner recommends completing the January 1, 2018 valuation using the current assumptions, then conduct the experience study in 2018, and ultimately use the updated assumptions for the 2019 valuation. One item that could change is returning the asset smoothing period to the more traditional five-year period. The funding method should also be reviewed to reflect consistency with GASB funding method. The funding ratio went down to 52.3%, primarily the result of lowering the discount rate to 6.5% from 7.5%.

Mr. Joyner also pointed out there are only 2,082 active participants in Group 1 (who were hired prior to September 1, 2005). This is the most expensive group and is no longer the largest group in the plan – it will continue to get smaller. Group 2 (hired between September 1, 2005 and December 31, 2015) now has 2,846 active participants. Their benefits are slightly smaller than Group 1, and the count will continue to decrease. There are 708 active participants in Group 3 (hired after 2015). They have the least costly benefit, and the count for this group will continue to grow as staffing increases.

Benita Ransom pointed out that there is another across-the-board salary increase coming in

April as well as an increase to the hourly minimum wage rate. Mr. Joyner indicated that these increases could have a similar effect on increasing the contribution amount after the 2019 budget year. As part of the experience study analysis, Mr. Joyner would like to know more of the salary expectations over the next five to ten years and include that information in the updated assumptions.

Mr. Joyner believes the funding percentage is at a low point due to the change in discount rate. The funding rate should improve with the additional contributions and improved benefit structure. If assets average a return 6.5% over the next ten years, then the funding percent will improve to 58%, and the contribution rate will remain approximately the same as it is now. Should assets return an average rate of 7.5% over then next ten years, then the funding percent would dramatically improve to almost 70%, and the contribution rate would drop to 13%.

Robert Robertson noted a significant number of retired participants in Group 1 with low benefits who could be positively impacted if the plan provided an increase in their benefit. It has been 12 years or longer for retired participants without any increase.

Ed Wall asked Mr. Joyner to comment on the fact that in previous years the contribution rate was based on budgeted payroll versus actual payroll, where budgeted payroll is almost always greater than the actual payroll. Mr. Joyner explained that through an agreement with the finance committee of the BOC (ERPS), Segal is now using the actual payroll amount to determine the county contribution rate. This will lead to a slightly higher contribution rate, and the dollar amount more closely resembles the actual salaries earned.

In meeting with the ERPS Committee in January 2018, Mr. Joyner described the impact of reducing the discount rate to 6.5%, which will increase contributions. He stated that the 6.5% discount rate is preserving the fund for the long term, protecting against market volatility, and locking into the higher contribution rate in a more systematic and progressive way. To build on that effort, Mr. Joyner recommends adoption of a funding policy defining how to best allocate resources for a variety of events and outcomes. Over the next several months, Segal will draft a funding policy and present it to the staff for review and discussion. The defined policy can be changed but it would force a public debate over those changes, presenting a more accountable structure. Robert Robertson indicated his desire of a stated policy and potentially defining an automatic periodic COLA increase. Mr. Joyner commends the board for making fiscally responsible decisions such as freezing the amortization period, moving to the 6.5% discount rate, and using the actual payroll amount for determining the contribution rate. He also commented that the County should have a full accounting of the remaining loan amount from the early retirement window when Segal completes the January 1, 2018 valuation.

Ed Wall described the process of interviewing two firms to conduct an audit of the pension plan. Mr. Wall has a long association with a staff member at Nichols, Cauley & Associates who performs similar audits for a number of local pension plans. Nichols, Cauley & Associates was also the lowest priced firm. Eric Hendrix motioned, Robert Robertson seconded, and the Board approved Nichols, Cauley, & Associates as pension auditor.

Eric Hendrix asked if participants who are eligible to buy back pension service are aware that they are buying back service into the Group 3 plan. Kenny Pinkerton responded that he has mentioned this to some of the applicants but not all of them. Mr. Hendrix indicated that the administration staff should find a way that clearly describes that the service purchased is allocated to the Group 3 plan. He also noted that the rates used in purchasing the prior service were more than the Group 3 rate. Mr. Pinkerton responded that in some years the rates were actually less than the Group 3 rate due to the changes in employee contribution rates through the years. He also clarified that the buy back rule applies only for those who previously received a refund. He agreed to add a statement to the buy back application to clearly communicate that the service purchased applies to the Group 3 formula.

Eric Hendrix motioned, David Littlefield seconded, and the Board approved the prior service buy back requests from Donald Bowden, Jr., a Watershed employee, Isaiah Simmons, a Watershed employee, Erin Spear, a Sanitation employee, Willie Swift, Jr., a Sanitation employee, and Steven Wells, a Fire Rescue employee.

Ed Wall asked for clarity around Timothy Wise's application to buy back previous service where he has been rehired twice. Kenny Pinkerton stated that he is eligible to buy back service only from the most recent rehire. In Mr. Wise's case, this is the period from August 30, 2006 to January 5, 2007. Eric Hendrix motioned, Robert Robertson seconded, and the Board approved the buy back application for Timothy Wise, a Sanitation employee.

Robert Robertson motioned, Eric Hendrix seconded, and the Board approved the leave of absence application for Stanley Peters, a Roads & Drainage employee.

Eric Hendrix motioned, Cornelius Yarbrow seconded, and the Board approved permanent disability for Mr. Angelo Brown, Sr.

By request from January 11, 2018 meeting, Ms. Sylvia Williams provided a statement of her Social Security disability benefit to the board. Dianne McNabb asked what made her Social Security benefit permanent. Robert Robertson responded that Social Security does not make her benefit permanent but the board has always treated disability applicants as being permanently disabled if they are approved for Social Security disability. Rocky Joyner confirmed that Social Security's approval for disability means it is permanent – Social Security does not approve temporary disability. Eric Hendrix motioned, Robert Robertson seconded, and the Board approved permanent disability for Ms. Sylvia Williams.

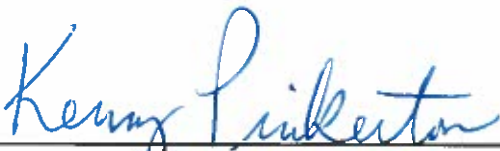
A public attendee asked about the increased contribution being attributable to lowering the discount rate to 6.5%. Ed Wall confirmed that. Mr. David Holcombe followed up by asking if that means the active employees will have to pay a larger contribution. Mr. Wall indicated that the Board of Commissioners (BOC) will have to decide how the cost is split between the employees and the county. The split has usually been between one-third and two-thirds up to sixty-fourth. Despite positive returns, the unfunded liability has increased every year for the past ten years, so the board felt as fiduciaries they had to force higher contributions and make some headway on the unfunded liability. The contribution increase is directed to the county,

but the BOC can decide what, if any, additional part is to be paid by the employees. Rocky Joyner commented that there are limits as to how much the employee portion can be. The Group 3 participants are very close to maxing out any additional contribution amount. The plan cannot charge participants an amount that is greater the value of their benefit. The employee contribution is different for each plan due to the different benefit formulas. Dianne McNabb asked about the source of the contribution rates for each group. Mr. Joyner indicated it came from Segal's study three to four years ago. Mr. Wall asked Mr. Joyner for a copy of the most recent report of how the employee contribution rates were derived for each group. Mr. Joyner indicated that it would cost \$4,000 to \$5,000 to update the study. Segal can include more information when they provide a quote on the experience study.

A public attendee commented that the county needs better communication about the pension plan, how it is funded, and how it benefits the employees, especially the younger ones.

Robert Robertson indicated that he continues to receive inquiries from many retirees asking about a cost-of-living increase and that it is necessary to lobby the BOC to approve a retiree increase. One BOC member indicated that a decision for a raise rests with the Pension Board and not the BOC. In the past, the Pension Board submitted a Home Rule amendment to the legal department which included an automatic annual one percent increase for the retirees so the BOC could have a chance to vote on it. The legal department determined that the request was illegal because it would put a cost on future administrations. This request should come before the BOC for a vote, and if the constituents do not like what their votes are, they could then vote for a BOC member who is more receptive to the needs of the retirees. Mr. Robertson requested that the Home Rule amendment be put before the BOC for a vote on automatic cost-of-living increases for retirees. The legal department can present their opinion but that should not preclude the BOC from hearing the request and voting. The Pension Board can work through any legal issues should the measure pass. Mr. Robertson reported that it is deceptive and not in good business practice for the BOC not to hear this request. This increase would be an annual budgeted item and will help the retirees cost increases such as medical insurance. The retiree medical plan is carved out separately from the active medical plan and the retirees are paying more for their coverage and it goes up approximately 10% per year. Mr. Wall indicated he will seek more information on how to present this request to the BOC.

With no further business the Board adjourned the meeting.



Kenny Pinkerton

Clerk, The DeKalb County Pension Board