Minutes

DeKalb County Pension Board

January 11, 2018

The DeKalb County Pension Board held a meeting on January 11, 2018 in the Board of Commissioners Conference Room. The following members were present: James Hendrix, David Littlefield, John McMullan, Dianne McNabb, Robert Robertson (via telephone), Cornelius Yarbro, and Edmund Wall. Others present: Deborah Brigham of Segal Consulting, Patricia Keesler of Benefits Law Group, Weston Lewis and Brad Penter of Callan Associates, Larry Jacobs, Kenny Pinkerton, Jay Vinicki, and Paul Wright.

Ed Wall called the meeting to order. John McMullen motioned, David Littlefield seconded, and the Board approved the November 9, 2017 minutes.

Cornelius Yarbro motioned, David Littlefield seconded, and Board approved payment of the following invoices.

Vendor	Service	Period	Amount
Montag & Caldwell	Investment Management	4Q 2017	$ 50,553.93
Southeastern Asset Mgt.	Investment Management	4Q 2017	203,502.00
		Subtotal	**$254,055.93**
ASM Consulting	Website Maintenance	November 2017	$ 300.00
Benefits Law Group	Legal Consulting	October 2017	1,530.00
Benefits Law Group	Legal Consulting	November 2017	5,068.50
Benefits Law Group	Legal Consulting	December 2017	5,248.50
Callan Associates	Investment Consulting	4Q 2017	20,500.00
Elarbee, Thompson, et al.	Legal Consulting – C	October 2017	174.00
Elarbee, Thompson, et al.	Legal Consulting – S	October 2017	4,623.73
Elarbee, Thompson, et al.	Legal Consulting – C	November 2017	657.50
Daniel Kingloff, MD	Disability Examination	December 18,	1,200.00
Segal Consulting	Consulting	Sept.-Nov. 2017	8,375.00
		Subtotal	**$47,677.23**
Total			**$301,733.16**

Brad Penter of Callan Associates provided a summary of the transition of assets from Montag & Caldwell to Loomis Sayles. The transition was completed by BlackRock who provided a summary of the transaction details, known as the "implementation shortfall," outlining their initial estimate of the costs vs. the actual costs. The final cost was $16,462, or 1.5 bps below the estimate, resulting in a favorable outcome for the fund. Transition expenses of $76,634 were more than expected, primarily due to unforeseen taxes on a French ADR investment. Opportunity costs related to the trading activity resulted in a gain of $60,172. The transition was completed on November 22, 2017.

Ed Wall questioned the increase in the pension funding drawdown amount, which was primarily related to the State Street balance in late December that did not reflect the January 1, 2018 retiree payments. Mr. Littlefield observed that the retiree payments each year exceed the employee contributions by approximately $60 million. Mr. Wall commented that the employee contributions, plus any earnings gains, are being used to fund the retiree payments. James Hendrix motioned, John McMullen seconded, and the Board approved $14.5 million funding ($6 million from Jennison, $4 million from Loomis, $2 million from Southeastern, and 2.5 million from Gabelli) for benefit payments in January-March 2018.

Weston Lewis indicated that no flash report at December 31, 2017 was yet available summarizing performance 2017 returns. Mr. Lewis announced that overall returns for 2017 were very good and that the funds also exceeded the benchmark indices. James Hendricks expressed concern that, due to the increased retiree payments, the plan is not making headway to reduce the unfunded liability. David Littlefield commented that the $60 million shortfall represents 6% of a $1 billion portfolio or 5% of a $1.2 billion portfolio.

Ed Wall referred to a meeting of the Pension Investment Committee on December 4, 2017 where modifications to Section 921 of the Pension Code were considered. He noted that Section Code 921 was established in 1945 outlining permitted investments at that time. Since then changes to the state law have introduced new choices of investment vehicles for public retirement plans such as private equity, hedge funds, etc. Any change to Section 921 of the Pension Code requires voter approval by the participants. Immediate voter action is not necessary and can take place in the next election cycle scheduled for January 2020. Weston Lewis summarized the need for making changes in the Code to clarify the permitted investment choices and remove the judgements involved in making market-related decisions. These changes allow for more flexibility in investment decisions yet keeps limitations and restrictions on securities that require scrutiny and in-depth trading knowledge. John McMullan questioned the insurability of the savings and loan provision, which only goes to $250,000. Mr. Wall replied that State Street sweeps up all cash and moves it to a money market fund that invests only in U.S. Treasury securities. Section Code 921 modifications include securities traded with capitalization in excess of $100,000 which are traded on a public exchange, bonds issued or secured or guaranteed by an agency of the U.S. government, collateralized mortgage obligations, bonds, and other indebtedness issued or guaranteed by any solvent institution provided the obligation is listed as investment grade by a national rating agency. It restricts prohibited short buys/sales, options buys/sells, private equity, foreign investments limited to 15% of portfolio, limit of 5% of portfolio in any one investment, limit of 3% in any one debt instrument, and all securities must be listed by a national rating agency. The Investment Policy will also be updated to include decision-making processes, asset diversification, use of prudent experts, best execution of transactions, asset monitoring, and avoiding conflicts of interest. Board members cannot accept anything of value from an outside entity. Mr. McMullen motioned, Cornelius Yarbro seconded, and the Board approved modifications to Section Code 921. This change will appear on the next public ballot for participant approval.

Ed Wall provided a summary of the plan discount rate assumption, indicating that many plans are lowering their discount rate to less than 7.5%. He noted that state law now allows plans to allocate a minimum of 25% of their assets in fixed income investments, down from 40%, in order to provide plans the best opportunity for financial gain. The Investment Committee met on December 4, 2017 to further consider lowering the discount rate to less than the current rate of 7.5%. Market assets in the actuarial valuation are averaged (smoothed) over 10 years and include losses in 2008 which yield a lower asset return than actual results. The valuation assets should improve the next few years when 2008 losses are not included in the average. All the contributions and investment gains are currently being used to pay retiree benefits, leaving no room to reduce the unfunded liability. The Investment Committee recommends lowering the discount rate assumption to 6.5% for a period of ten years, thereby requiring a larger contribution from the county to fund the plan. If the investment returns during that time warrant a return rate of 7.5% or more, the Board can restore the discount rate to 7.5% and doing so, the funded status has the potential to improve from the current rate of 60% to 75%.

Deborah Brigham described a ten-year projection of the discount rate change contrasting the current 7.5% rate against those with: (a) a discount rate of 6.5% and earning 6.5% vs. (b) a discount rate of 6.5% and earning 7.5%. Returning the assets to full market value in the tenth year with a return of 7.5% would create a funded status of 73%, a contribution rate of 12%, and the unfunded amount would decrease to $597 million.

Ed Wall shared that the county contribution rate for 2017 was 15% and the county contributed 18%. The 3% difference will be used to retire almost all the amount the county borrowed to pay for part of the 2010 early retirement window. In December 2017, the Board of Commissioners approved the minimum contribution rate of 16.56% for 2018 using the current 7.5% rate. Lowering the discount rate to 6.5% would require a 21% contribution rate, an increase of approximately $12 million. This is expected in what the Pension Board is trying to achieve to contribute more to the plan. The county would have to cut expenses, raise taxes, or pursue a combination of both.

Jay Vinicki indicated that the increased contribution amount under the 6.5% rate would be hit to the county and affect discretionary spending elsewhere. Ed Wall reached out to BOC members – Nancy Jester indicated it was time to contribute more to the plan, Kathy Gannon liked the idea but suggested a phase-in increase, and Jeff Rader indicated more discussion was needed.

Mr. Vinicki indicated the decision to contribute 16% resulted from the county's desire to create more stability before taking on additional expenses. Robert Roberson voiced concern over the unfunded level and requests support for moving to the 6.5% discount rate to trigger additional funding. Mr. Wall expressed a desire to gain input from the CEO before advancing. Robert Robertson interjected he understands the desire for input from everyone, but the response from the CEO's Office in the past inquiries has been less than positive. The Board is independent from the county, has a responsibility to make the fund financially sound, and does not have to consider the budgetary concerns of the county, stressing that the Board should make a decision in today's meeting.

John McMullen asked Weston Lewis what the fund's return has been for ten years. It has been around 6.8% for the last ten-year period. For 25 years, it has been 8.95%. Mr. McMullen asked Ms. Brigham if the Board is are required to use the assumed rate vs. the actual rate. Ms. Brigham indicated the Board needs to use an assumed rate to discount future plan benefits, and differences in the asset returns are reflected in the gains and losses each year. Mr. McMullen stated that the 25-year return of 8.95% on assets was a better indicator of performance than the ten-year return due to the skewed losses incurred in 2008. He favors going to 7.0% vs. 6.5%, contrasting the assumed rate vs. what the fund is actually returning. Ms. Brigham indicated the Board is not allowed to use unrealistic assumptions – 6.0% to 7.5% is a realistic rate in today's environment. The most recent national survey indicated an average of 7.52%. Mr. Lewis stated that the ten-year return average will increase substantially when 2008 is not considered. Mr. Littlefield stated that looking retrospectively at returns is limited and does not reflect what the fund will return in the future and the Board needs a tighter range. Mr. Wall stated that he is driven by the fact that the unfunded liability has increased every year in spite of significant market asset returns and wants to find a way to contribute more to the plan. He suspects a down year somewhere in the next three years and wants to force a way to contribute more to make a dent in the unfunded liability. The only options are to earn more or contribute more. Diane McNabb inquired about the possibility of a staggered approach of lowering the discount rate. Ms. Brigham indicated this is possible to do and other neighboring counties are doing this. Mr. Vinicki indicated that a $12 million contribution would exhaust all increases in the budget. The county is looking at whether to issue more bonds for water and sewage improvements. Mr. Wall claimed that going to 6.5% would indicate to Moody's that the county is serious about making headway on their pension funding. The rating agencies would expect the county to raise the necessary funds to meet the pension funding.

Ed Wall indicated his desire to notify the CEO's office of this change rather than be heavy handed in making the request. Robert Robertson recommends a vote now for the 6.5% rate change. James Hendrix made a motion to reduce the discount rate to 6.5%. Motion was seconded by Cornelius Yarbro. David Littlefield made a substitute motion to reduce the discount rate to 7.0%, seconded by John McMullen. Using Robert's Rules of Order, the Board must resolve and vote on the substitute motion first. Ms. Brigham indicated using the 7.0% rate the plan would obtain a funded status of 68% and contribution rate of 19.25% in 2019, about half the contribution increase as the 6.5% rate. Mr. Robertson stated his option to vote electronically via phone. A vote on the substitute motion was made as follows: Ed Wall, John McMullen, and David Littlefield voted for and James Hendrix, Cornelius Yarbro, and Robert Robertson voted against. Thus, the substitute motion for a discount rate of 7.0% failed, due to a tie. A vote was exercised on the original 6.5% motion was made as follows: Ed Wall, James Hendrix, Cornelius Yarbro, and Robert Robertson voted for; John McMullen voted against; and David Littlefield abstained. Thus, the original 6.5% motion passed.

Ms. Brigham confirmed that 6.5% should be used on the actuarial valuations going forward.

A sample statement of asset monitoring was provided by State Street but the Board agreed it is not worth the expense of utilizing their service. The new asset displays recently provided by Callan in the quarterly reports are sufficient to monitor assets going forward.

John McMullen motioned, James Hendrix seconded, and Board approved not to retain Bates Carter for the 2017 audit and to solicit RFP's to find a replacement auditing firm. An independent audit firm must be identified that is not tied to the county audit process. RFP's will be solicited and three potential recommendations will be provided prior to the March 2018 meeting.

James Hendrix motioned, Cornelius Yarbro seconded, and Board approved the prior service buy back requests from Bionka Jones, a Sheriff's Office employee, and Trumondia Williams, an employee of the Law Department.

Public comments from Gayle Walldorff included an inquiry as to how the $12 million loan amount to the county was paid off. Ed Wall replied that the loan to the county from the plan was derived from 2010 Early Retirement Window to pay a special benefit in lieu of Annual Leave time to retirees included in the window, at a rate of 7.5% interest. An amortization schedule was approved for the payments over 30 years. All county departments participated in the cost sharing, and actuarial costs recognized the payments. For 2017, the minimum contribution amount was 15% but the Board of Commissioners approved to keep the contribution rate at 18%, applying additional amounts toward the unfunded shortfall. Jay Vinicki determined that the extra 3% amount could be used to pay the loan amount and paying it off was the best course for the county, although there could be a small part still remaining. The loan proved to be the best fixed income asset since 2010. Ms. Walldorff further asked if the Board would consider indexing and passive investments as a modern way of investing. Mr. Wall commented that indexing and passive investing has been around for some time. Mr. McMullen stated his view of responsibility as one choosing the money managers who are the experts to choose the investments vs. an indexed approach where he would then be choosing the investments and thus, he is not comfortable with an indexing investment strategy. Mr. Wall confirmed there was a time where the manager fees were not advantageous to the performance returns the fund was receiving but over time, and even more recently in 2017, the money managers have returned a better performance gain than a pure indexing strategy. The estimated fee savings of $3.5 million a year utilizing an indexing strategy may be made up or exceeded by an active trading strategy or it might return less. There is no right or wrong answer but the Board has determined that an active strategy is best at this time. Ms. Walldorff also inquired as to what participants can expect in the way of communication for upcoming changes to the Code. Ed Wall replied that a flyer mailing was most reasonable to explain the changes and why the Board is proposing the changes. The changes needed are to remove some the investment judgement calls by clearly defining the permitted investment choices.

Public comments from Jonathan Weintraub included an inquiry about the status of a cost-of-living increase for the retirees. Ed Wall responded that the Board presented a request to the Board of Commissioners for a 2% COLA increase, amounting to approximately $1.6

million increase in retirement payments. The December 15, 2017 budget does not include any COLA, and the Board's decision today approving the 6.5% discount rate had no bearing on the December 2017 budget. Robbie Robertson commented that the Board had done everything possible to present on-going COLA requests to the Board of Commissioners, including an automatic 1% increase each year.

Public comments from an employee inquired about the need for on-going education of his staff and other colleagues about the pension benefit. The employees are contributing a lot of their money to the plan, and they want to know more about how it is going to benefit them.

Public comments from a retired attendee expressed appreciation to the Board and to Robert Robertson for his efforts in representing the retiree participants.

Public comments from a retired attendee indicated he has received only one increase in 17 years and encouraged the Board to continue working toward a COLA.

The Board moved to Executive Session to discuss disability applications and renewals.

Upon returning from Executive Session, James Hendrix motioned, Cornelius Yarbro seconded, and Board approved a 12-month disability benefit for Alvin Harper.

James Hendrix motioned, Cornelius Yarbro seconded, and Board approved a 12-month disability benefit for Thomas Simmons Jr.

James Hendrix motioned, Cornelius Yarbro seconded, and Board denied continuing disability retirement benefits to Thomas Jones.

James Hendrix motioned, Cornelius Yarbro seconded, and the Board delayed continuation of the disability benefit for Sylvia Williams, pending verification of her Social Security benefit.

With no further business the Board adjourned the meeting.

Kenny Pinkerton

Kenny Pinkerton
Clerk, The Dekalb County Pension Board