CITY OF PORT ORANGE
POLICE OFFICERS' PENSION BOARD
FEBRUARY 19, 2016

The Port Orange Police Officers' Pension Board of Trustees held its quarterly meeting on Friday, February 19, 2016 in the Second Floor Conference Room of City Hall, 1000 City Center Parkway, Port Orange, Florida.

MEMBERS PRESENT:
Chairman Steve Braddock (police member)
Secretary William Proctor (police member)
Warren Carman (fifth member)
Drew Bastian (resident member)
Brian Cobb (resident member)

CONSULTANTS:
Ken Harrison, Board Attorney – Sugarman & Susskind
Dustin Watkins, Associate Attorney – Sugarman & Susskind
Charlie Mulfinger, Investment Consultant – Graystone
Scott Owens, Investment Consultant - Graystone
Chad Little, Actuary – Freiman Little Actuaries
Karan Rounsavall, Plan Administrator

Chairman Braddock called the meeting to order at 9:01 a.m. A quorum was in attendance. Board members welcomed Brian Cobb, new resident member, who filled the vacancy created by the resignation of Trustee Todd Traster in early January.

APPROVAL OF MINUTES

Member Bastian moved to approve minutes of quarterly meeting November 20, 2015 as submitted. Member Proctor seconded the motion and it carried unanimously.

OFFICER AND TRUSTEE REPORTS - *None*

CONSENT AGENDA

The following items were presented for action as recommended:

A. Approve plan expenditures as follows:
   1. Sugarman & Susskind – monthly retainer for November 2015 - $2,000. *Recommendation:* Ratify payment.
   2. Sugarman & Susskind – monthly retainer for December 2015 - $2,300. *Recommendation:* Ratify payment.
   3. Sugarman & Susskind – monthly retainer for January 2016 - $2,300. *Recommendation:* Ratify payment.
   4. Plan Administrator Karan Rounsavall – monthly fee (November 2015, December 2015, January 2016) - $7,200. *Recommendation:* Ratify payments.
   5. James Moore, CPA – progress billing for audit of 9/30/2015 financial statements through December 2015 - $4,500. *Recommendation*: Ratify payment.
   6. James Moore, CPA – progress billing for audit of 9/30/2015 financial statements through January 2016 - $3,000. *Recommendation*: Ratify payment.

7. Florida Public Pension Trustees Association (FPPTA) – 2016 annual dues - $600. *Recommendation:* Ratify payment.
8. Florida Public Pension Trustees Association (FPPTA) – Registration for winter trustees school for Drew Bastian and Warren Carman - $900. *Recommendation:* Ratify payment.
9. Hilton Orlando – lodging expenses for trustees to attend FPPTA winter school - $1,100. *Recommendation:* Ratify payment.
10. Florida Public Pension Trustees Association (FPPTA) – registration fee for Certified Public Pension Trustee Program for Warren Carman - $900. *Recommendation:* Ratify payment.
11. Warren Carman – reimbursement of travel expenses for attendance at State's Pension Trustee Conference in Orlando - $409.04. *Recommendation:* Ratify payment.
12. Graystone Consulting – Tampa – all-inclusive investment fees (October 1, 2015 through December 31, 2015) - $62,222.16. *Recommendation:* Ratify payment.

B. Acknowledge refund of member contributions to the following non-vested members:

1. Ashley Kortright (non-vested member) in the amount of $1,543.29. *Recommendation:* Ratify refund as stated.
2. Ray Chan (non-vested member) in the amount of $14,376.71. *Recommendation:* Ratify refund as stated.

C. Acknowledge distribution of DROP account balance for John Jakovenko as of February 1, 2016. *Recommendation:* Ratify distribution of DROP account balance to Retiree John Jakovenko.

Member Carman moved to approve all consent agenda items as recommended. Member Proctor seconded the motion and it carried unanimously.

CONSULTANT REPORTS

A. Chad Little – *Freiman Little Actuaries, LLC* (Plan Actuary)

1. Presentation of annual actuarial valuation for fiscal year ending September 30, 2015

Actuary Little distributed the October 1, 2015 Actuarial Valuation Report for the Port Orange Police Officers' Pension Plan. This report established the annual City contribution to the Pension Plan for the fiscal year ending September 30, 2017. The City's minimum required contribution, expressed as a percentage of payroll, was 66.03 percent; expressed as a dollar amount, the cost was $3,217,965 (city and state contributions combined). The cost decreased from the previous year when expressed as a percentage of payroll but increased as a dollar amount. Mr. Little stressed that the Pension Plan was not *underfunded* as the City of Port Orange had always made its required contribution and in some years contributed more than required in order to pay down the unfunded liability. The Plan's funded status was 65.30 percent, representing a small increase over the previous year's funded percentage of 63.97 percent.

The investment return on the "market" value of assets was a negative (0.1) percent; the return on the "actuarial/smoothed" value of assets (five-year smooth) was 7.0 percent which was less than the 7.65 percent assumed net investment rate of return. Mr. Little noted that asset values were smoothed over a five-year period to reduce year-to-year volatility. Over the past ten years, the average market value return on assets was 5.4 percent. Investment returns less than the assumed rate of return resulted in increased annual minimum required contributions in the future.

The unfunded accrued liability (UAL) was $15,573,818. Effective with this valuation, the UAL was amortized over a 25-year period. The Plan used the RP-2000 Combined Mortality Table with Scale AA, however as of the October 1, 2016 valuation, the Plan needed to utilize the same mortality table used by Florida Retirement System.

The valuation report also included required disclosures under *Florida Statutes* 112.664(1). Report disclosures required by Governmental Accounting Standards Board (GASB) 67 and 68 were provided as a supplemental report.

Member Proctor moved to approve the 2015 actuarial valuation report as presented. Member Bastian seconded the motion and it carried unanimously. Plan Administrator Rounsavall would submit the approved valuation to the State Division of Retirement.

At this time the Board recognized Citizen Ted Noftall who questioned the City's overpayment of $1.1 million into the pension fund and wondered if this was to mask underlying problems. Actuary Little advised that excess contributions were used to pay down the unfunded liability; this was money that would be contributed to the fund eventually.

2. Declare expected annual rate of investment return for assets of Port Orange Police Officers' Pension Plan for short term and long term thereafter in accordance with Section 112.661 *Florida Statutes*

Board members sought input from their actuary and investment professional as to an expected investment rate of return going forward. Actuary Little was comfortable with the current 7.65 percent expected investment rate of return. Mr. Mulfinger felt that 7.65 percent was an acceptable rate of return but questioned whether or not it could be achieved over the next five years given the current low interest rate environment for fixed income investments. He favored lowering the rate of return assumption over time.

Per the Board's previous direction (September 3, 2016), the actuary would prepare the 2016 valuation using 7.55 percent as the assumed annual rate of return.

Member Bastian moved to declare a 7.65 percent expected rate of return for retirement plan assets going forward. Member Cobb seconded the motion and it carried on an all yes vote.

B. Zach Chalifour – *James Moore CPA* (Auditor)

A. Presentation of draft audit of Port Orange Police Pension Fund financials for fiscal year ended September 30, 2015

Mr. Chalifour presented the audit which was complete pending inclusion of schedules from the now approved annual actuarial valuation. This was the second year that his firm had performed the audit for the Police Pension Fund and observed continued improvement in operations and attention to detail. At this time, his firm presented an *"unmodified opinion"* of police pension financials for Fiscal Year 2014/2015 which was the highest standard.

The audit was performed in conformance with governmental auditing standards. Mr. Chalifour advised that $3.4 million of "new" money came into the plan. There was a "net" investment loss for the fiscal year given investment-related expenses of $241,340. He also noted that there were four substantial DROP payouts during the year.

Plan Administrator Rounsavall asked Mr. Chalifour to provide a breakout of administrative expenses for her use in preparing the detailed accounting report for the State. Mr. Chalifour agreed to do this.

The audit report also presented recommendations and comments for improving the Plan's efficiency and internal controls. In the previous year's audit, there were eight such comments/recommendations; four of these comments were satisfactorily addressed during the past year (to-wit: benefit election form, definition of year as *"plan"* year, periodic review of service providers, and treatment of after-tax participant contributions). Mr. Chalifour was pleased with the substantial progress made along this line. Four repeat comments remained as follows:

2015-01 Preparation of Financial Statements

This was a standard comment for smaller agencies and a recommendation to engage the services of accounting firms to draft financial statements should be considered from a cost/benefit standpoint. The General Employees' Pension Plan received a similar comment. This was not a major concern.

2015-02 Document Retention and Retiree Files

Mr. Chalifour noted that files for ten retirees still could not be located, thus initial payment amounts could not be verified. The missing files were for participants who had retired many years earlier (prior to 2000).

2015-03 Creation and Maintenance of Policy Manual

The audit noted that the Pension Plan continued to actively set policies/procedures through formal board action. Mr. Chalifour recommended that these policies be summarized in a manual and reviewed on an annual basis. Plan Administrator Rounsavall noted that this was a work in progress.

2015-04 Monthly Financial Statement Review

Again, this comment should be considered from a cost/benefit standpoint and was not a major concern at this time.

Member Bastian moved to accept the audit report for the fiscal year ended September 30, 2015 as presented. Member Carman seconded the motion and it carried unanimously.

C. Charles Mulfinger and Scott Owens – *Graystone Consulting/Morgan Stanley Wealth Management* (Investment Consultant)

1. Performance Report for quarter ended December 31, 2015

Mr. Owens delivered a brief economic overview adding that markets had been difficult since the end of the quarter. Recent volatility was triggered by macroeconomic and geopolitical concerns including China's devaluation of its currency and falling oil prices. For the quarter ended December 31, 2015, growth stocks outperformed value stocks in both large and small capitalization categories. While most sectors were positive, energy stocks were clearly the laggard. Large capitalization stocks outperformed small, particularly Facebook, Amazon, Net-Flix, and Google (FANG). In the fixed income category, high yield bonds underperformed but high quality issues held their own and would protect the portfolio if the economy took a downturn. Graystone predicted very slow economic growth but did not believe that the markets were headed toward a global recession. Graystone produced lower returns with less risk but had added value over time.

Mr. Mulfinger continued with a review of the Investment Performance Report for the first quarter of Fiscal Year 2015/2016. The Fund was up 2.52 percent on a time-weighted basis (net of fees) which trailed the policy index which was up 3.10 percent. Total market value as of December 31, 2015 was $28,307,776.84 representing a gain of $756,737.91 (net of fees) since the previous quarter ended September 30, 2015. The trailing one-year return was positive 1.03 percent (net of fees) which slightly exceeded the policy index return of a positive 1.00 percent but fell short of the 7.65 percent assumed actuarial investment rate of return. As of February 16, 2016 the market value of the fund was $26,656,720 (a loss of 2.7 percent since September 30, 2015).

Quarterly performance results (gross of fees for quarter ending December 31, 2015) for the various investment styles/managers represented in the portfolio were as follows:

BlackRock (large cap value) – positive return of 7.42%*
Jennison (large cap growth) – positive return of 8.75%*
Wedgewood (large cap growth) – positive return of 2.56%
Connors (large cap core) – positive return of 5.13%
GW Capital (small cap value) - positive return of 2.17%
RBC (small cap growth) – positive return of 4.81%*
Lazard (international value) – positive return of 3.84%
Renaissance (international growth) - positive return of 6.11%*
Madison Investment Advisors (fixed income) – negative return of (0.39%)*
Pine Grove (alternative investments – hedge fund) – negative return of (1.57%)
Private Advisors (alternative investments – hedge fund) – negative return of (2.01%)
UBS (private real estate) – positive return of 3.01%*
* These managers beat their respective fund index.

Total fees paid to Graystone Consulting for the quarter were $62,222.16 which included consulting, trading, and custody as well as fees charged by the individual managers. Hedge funds were reported net of fees.

Mr. Mulfinger reviewed the compliance checklist which examined the portfolio against the Board's Investment Policy Statement (IPS) for each asset class, concentrating on those managers reporting a "No." He commented specifically on the drastic underperformance of Connors (large cap core), noting that they were a contrarian manager whose performance should rebound when the energy sector improved. There was no need to rebalance the portfolio at this time.

Member Bastian moved to accept the investment performance report as presented. Member Proctor seconded the motion and it carried unanimously.

2. Small and Mid-Capitalization Value Investment Manager Search

Mr. Mulfinger and Mr. Owens discussed the fact that GW Capital (the Pension Fund's small cap value manager) was closing its investment firm as of March 31, 2016. It was unusual for a firm with sizeable assets under management to close its operations; nonetheless, it created the need to hire a new manager along this particular investment style. Mr. Owens recommended that the Pension Board consider a small/mid-capitalization value manager to replace GW Capital; Graystone vetted several investment managers in this style.

Board members were in receipt of a comprehensive investment manager search analysis prepared by Graystone Consulting along with a summary sheet comparing fees, returns, risk and other considerations.

Following brief discussion, Member Cobb moved to select Boston Partners for its small/mid-capitalization value investment manager to replace GW Capital. Member Bastian seconded the motion and it carried unanimously.

D. Ken Harrison – *Sugarman & Susskind* (Attorney)

Attorney Harrison gave a brief legislative update. No bills were introduced during the session that affected local law plans at the present time.

Attorney Watkins reported on new Internal Revenue Service rulings which involved in-service distributions and normal retirement age. As the Port Orange Police Pension Plan did not allow in-service distributions, it was unaffected by these rulings.

E. Karan Rounsavall – Plan Administrator

1. Discuss action plan related to non-taxable contributions made by retired members

Plan Administrator Rounsavall recently met with Zach Chalifour (auditor) and Jamie Miller (Port Orange Budget Analyst and former Payroll Coordinator) concerning the treatment of after-tax contributions made by plan participants/retirees. Prior to October 1, 1993, deductions for contributions to the pension plan were made on an after-tax basis. Subsequent to that date, contributions were deducted on a pre-tax basis. Thus, any participant that was hired prior to October 1, 1993 made contributions to their pension plan that was already taxed. Pursuant to Internal Revenue Code guidance, it was appropriate to determine what portion of a retiree's monthly benefit was non-taxable based on the total after-tax contributions made prior to October 1, 1993.

This non-taxable calculation was performed for a number of current retirees, however, the plan administrator's review of retiree files revealed that there were several others for whom the calculation was never performed. Further, of those calculations that were performed, many were incorrect and, in fact, overstated because they were based on total contributions which clearly represented more than just after-tax contributions. Unfortunately, the City only had payroll records that captured after-tax contributions made by participants from January 1, 1990 through October 1, 1993. Both Mr. Chalifour and Ms. Miller agreed that there were inconsistencies and overstated non-taxable calculations for a number of current retirees. However, there were no records available at this time to determine the correct non-taxable benefit.

Plan Administrator Rounsavall proposed a three-part action plan supported by the auditor and budget analyst as follows:

(1) Acknowledge inconsistencies and likely overages in reported after-tax contributions for some current retirees and thus a higher non-taxable portion of their total monthly benefit;

(2) Proceed with actuarial calculation of non-taxable portion of monthly benefit for those retirees with after-tax contributions between 1990 and 1993 for which reliable and verifiable data was available; and

(3) Prepare correspondence to retirees who purchased prior service (military or law enforcement) to advise that their contributions paid to the pension plan for this purchase might be non-taxable and to consult their tax advisor for further advice.

It was noted that none of these recommendations affected the overall pension plan as gross monthly distributions to retirees were unaffected.

Member Bastian moved to proceed with the action plan to address non-taxable contributions to the police pension plan as stated above. Member Carman seconded the motion and it carried unanimously.

2. Educational opportunity – Annual Police Officers' and Firefighters' Pension Trustee School in Tallahassee (May 16 – 18, 2016)

Mrs. Rounsavall announced the upcoming trustees' school. If any member wished to attend, they were to contact her at their earliest opportunity for registration information, reservations, etc.

OLD BUSINESS – None

NEW BUSINESS

A. Request of disability retiree (line-of-duty) for letter from Plan Attorney advising that line-of-duty disability benefits were non-taxable distributions and for corrected 1099-R's for 2012, 2013, 2014, and 2015 to that effect

Plan Administrator Rounsavall was contacted by one of the Pension Plan's disability retirees who was having difficulty with his federal income taxes and communication with the Internal Revenue Service because the coding on his 1099-R identified distributions as "taxable amount not determined." He requested a letter from the plan attorney to the effect that line-of-duty disability benefits were non-taxable distributions along with corrected 1099-R's for 2012, 2013, 2014, and 2015 to assist with his filing amended tax returns for those years.

Member Bastian moved to direct the attorney to prepare a letter advising that line-of-duty disability benefits were non-taxable distributions and to direct the plan administrator to contact First State Trust Company (fund custodian) for corrected 1099-R's for the stated prior years to reflect no taxable income. Member Carman seconded the motion and it carried on an all yes vote.

Going forward, Member Bastian moved that 1099-R coding for all line-of-duty disability retirees in the Port Orange Police Pension Plan be coded similarly and reflect no taxable income. Member Cobb seconded the motion and it carried on an all yes vote.

B. Discussion and recommended action to clarify treatment of *"breaks in service"* as it relates to vesting in the retirement plan

Board members were in receipt of Attorney Harrison's February 17, 2016 correspondence setting forth his legal opinion related to interruption in service and loss of vesting credits. Based on Sections 54-125 and 54-112 of the plan document, the attorney opined that a plan participant was not entitled to earn service credit in the Port Orange Police Pension Plan during any period that they were not actively employed and making contributions. There was no provision for the participant to subsequently make contributions to the plan for the period of interrupted service.

A break in service did not occur if a member left employment and kept his contributions in the plan and subsequently returned as a full-time employee. A participant would retain all accrued credited service prior to the interrupted service.

Member Proctor moved to accept the attorney's legal opinion as stated in the February 17, 2016 correspondence. Member Carman seconded the motion and it carried on an all yes vote.

C. Ratify early retirement benefits for Serena Besuden as of November 1, 2015 (Ten-Year Certain and Life Annuity)

Member Bastian moved to ratify early retirement benefits for Serena Besuden as of November 1, 2015 based on her selection of the Ten-Year Certain and Life Annuity which provided a monthly benefit of $1,773.25 based on her total credited service of 13.25 years. Member Cobb seconded the motion and it carried unanimously.

PUBLIC COMMENT - None

ADJOURNMENT

The meeting adjourned at 12:15 p.m.

Steve Braddock, Chairman

Karan Rounsavall

Karan Rounsavall, Plan Administrator