Tulare County Employees' Retirement Association

Pension Progress

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Keeping Members Informed Volume 16, No. 3 September, 2015

Investment Markets Disappoint in 2014-15

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As we have written in previous notes, the global economy has been kept afloat by record amounts of monetary stimulus from the world's central bankers. Here in the U.S., it has been nearly 10 years since the Federal Reserve has raised interest rates. Many experts believe the Fed will finally begin to reverse course, and begin slowly raising rates by the end of 2015.

This increase was supposed to be a sign of strength for the world's largest economy, as the U.S. has and continues to demonstrate modestly improving conditions with unemployment coming down and GDP growth in the 2-3% range. Unfortunately, there is some concern that a rate increase could negatively impact capital markets around the world, as global growth already appears to be slowing. The concern centers on the uncertainty of a rate hike's impact on a strengthening dollar, already fragile commodity prices, and associated deflationary pressures.

In the latest cycle, commodity prices have declined precipitously, led by the price of oil, which dropped to under $40 per barrel in August. This drop has negatively impacted several emerging market countries, where oil and other commodities are the main exports. Further, China's stock market has been highly volatile despite the Chinese government's attempts to intervene. Finally, it isn't only China's stock market that is experiencing heightened volatility. U.S. stock markets have also experienced an uptick in volatility, causing investor concern despite many reasonably robust economic indicators.

The bottom line for the global economy and investment markets is that global growth is slowing from moderate levels, and the record amount of monetary stimulus has not gotten us out of the woods.

Within this backdrop, the Plan's investment performance has come off the highs of the last several years. For the current fiscal year, the Plan returned just 0.9%, net of management fees. While returns were subdued for the fiscal year, the longer-term picture remains favorable. Over the last three and five-year periods, the Plan averaged a 9.6% annual return, comfortably above the Plan's target return.

For the latest fiscal year, international equities rebounded during the first half of the 2015, but it wasn't enough to overcome the losses in the second half of 2014. Investments in international equity was one of the major headwinds for the Plan with a return over the fiscal year of -5.8%. Although commodity investments make up less than 5% of the portfolio, they also detracted from total portfolio returns given the pullback in oil and the strengthening of the U.S. dollar. The Plan's fixed income allocation was generally flat, returning 0.6% over the fiscal year. Domestic equities were stronger with a return of 8.6%, and real estate was the real star for the year, returning 14.8%.

In the midst of periods of heightened volatility like the one we are currently experiencing, it is important to keep in mind that TCERA is a Plan with a very long-term investment horizon. This allows the Plan to take advantage of market risk in order to generate higher long-term returns. Along the same lines that we can't expect uncommonly high returns every year, we also shouldn't expect persistent below average returns either. The key is to remain disciplined and adhere to the long-term investment strategy laid out in the Investment Policy. *(Continued on next page.)*

What Is The Board Of Retirement?

The Tulare County Employees' Retirement Association (TCERA) functions under the provisions of those sections of the California Government Code known as the "County Employees' Retirement Law of 1937" (or '37 Act). One of the purposes of the '37 Act is the establishment of a "Board of Retirement" to oversee the retirement plan. In Tulare County, the Board of Retirement consists of nine members. Four of these individuals are appointed by the Board of Supervisors, two are elected by General plan members, one is elected by Safety plan members, one is elected by retirees, and the final member is the County Treasurer. Alternate Board members can also be elected or appointed to serve in the absence of the regular Retiree member, the Safety member and the Treasurer. All Board members (except the Treasurer) serve for three year terms and then have to be re-appointed or re-elected in order to continue serving on the Retirement Board.

Board members are also referred to as "Trustees" and are responsible for the retirement plan and for those amounts that are held in trust for the plan members. Board members have a fiduciary relationship with plan members (employees and retirees of Tulare County and TCERA's other plan sponsors). Retirement Board members have a wide variety of responsibilities to the plan and plan members. Several of these duties are described in the California Constitution. One of these sections reads:

"Members of the Retirement Board of a public or retirement system shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. A Retirement Board's duty to its participants and their beneficiaries shall take precedence over any other duty."

To fill their fiduciary responsibilities, Board members must address issues related to investment of the funds in the retirement plan, approve an annual administrative budget for the Retirement Office, as well as conduct and approve studies impacting employer and employee contribution rates. The Board approves service retirement benefits and takes action on applications for disability retirements. It seeks to establish educational programs and materials to better inform plan members of the structure and benefits of the retirement plan and to hire competent staff to assist in accomplishing the goals and objectives of the Retirement Board.

Given the wide-range of duties and responsibilities, the Board of Retirement is in a unique position to administer the retirement plan on behalf of the plan participants and plan sponsors. The mixture of County appointed members and employee elected members allows the Retirement Board the opportunity to consider all sides prior to making decisions impacting the long-term health of the Retirement Association. The Board of Retirement generally meets on the second and fourth Wednesdays of each month at the TCERA Offices. The general public is welcome to attend all meetings of the TCERA Board of Retirement.

Investment Markets…

(Continued from 1st page.)

That said, opportunities to upgrade the portfolio are continually being evaluated. This year, the Board decided to replace one of the Plan's fixed income managers due to organizational turnover. Also, the plan is currently considering additional investments in private equity and hedge funds to bring those allocations up to policy targets. Finally, the plan conducted an asset allocation review in late September to evaluate the merits of adjustments to the current investment program. We expect all these alterations will improve investment performance over time and help the portfolio meet its long-term return objectives.

FAQ's

Q. I just got divorced. Why did my ex-spouse get part of my retirement account?

A. California is considered to be a **community property** state and retirement benefits earned during the marriage are a community property asset. When a plan member and their spouse divorce, the Retirement Office will divide the account based on the instructions provided in the **Domestic Relations Order** or **Final Judgment** in the dissolution of marriage. Normally *(but not always)* the portion of retirement benefits earned during the marriage is split 50-50.

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How Is My Pension Contribution Calculated?

As any member of TCERA is aware, retirement contributions are taken from employees. But not all employees contribute into the plan at the same rate. Why? There are many factors that determine the rate of contributions an individual will pay into the plan. The key elements are the following:

Membership type:

Members of TCERA fall into one of two types: Safety and General. Simply stated, Safety members are those individuals whose primary job duties include law enforcement or fire suppression. General members are everyone else. Safety members have higher benefit formulas than do General members, but they also pay higher rates of retirement contributions than do their General member counterparts. (The Employer also pays a higher contribution rate for Safety members than what is paid for General members.)

Tier:

The Board of Supervisors has approved different tiers of benefits for members of the TCERA plan. Membership in a particular tier is dependent upon when the person joined TCERA and **not** necessarily when the County or other plan sponsor first employed the individual. Leaving the plan and withdrawing your funds means that you will be in a later tier should you return to membership at a future date. (But you have the option of "buying back" your previous service credit and tier if you decide to do so.) Members of Tier I have the highest level of retirement benefits. Tier I members are those people who joined TCERA on or before December 31, 1979. You are a Tier II member if you joined the plan from January 1, 1980 through December 31, 1989 and a Tier III member if you joined TCERA on January 1, 1990 or later. Tier II and Tier III members have the same retirement benefit formula.

Effective January 1, 2013, the Public Employees Pension Reform Act (PEPRA) set new requirements for retirement benefits and eligibility in California. This has led to another retirement benefit tier (Tier IV) that was approved by the Tulare County Board of Supervisors and impacts all TCERA plan members who joined the plan as of January 1, 2013 or later who do NOT have reciprocal membership with another qualified retirement system.

Age at entry:

The laws governing TCERA are written with the expectation that plan members will contribute funds into the plan to pay for a portion of their retirement. In order for plan members to pay a somewhat equal amount towards the pension amounts they will eventually receive, member retirement contributions are based not only on the individual's membership type and tier, but also on the age of the employee upon entry into the TCERA plan. A person who is younger (let's say 25) when she enters the plan will need to contribute less on a pay period-by-pay period basis than will a person who is 45 when he enters the plan. That's because the 25 year old has much more time to accumulate the funds needed by the expected age of retirement. As a result, your age at entry plays a key role in determining your individual rate of contributions into the retirement system.

Employee contribution rates are reviewed as part of an ***actuarial study (or "valuation")*** that is conducted by TCERA each year. The study reviews several economic and demographic factors pertaining to the TCERA plan such as investment returns, levels of employee compensation, mortality rates, service and disability retirements, etc. Both employee and employer contribution rates can change based on the results of the actuarial valuation.

While no one enjoys paying retirement contributions out of their pay, employee and employer contributions play an important role in making sure that the pension benefit promises can be met for current and future TCERA plan participants.

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TCERA Responds to Frequently Asked Questions

Q. I'm planning to retire at the end of the year. How can I avoid paying a lot of taxes on my sick leave and vacation time payoffs.

A. One way may be to delay your effective date of retirement into the next calendar year. By retiring at the end of the year you will not only have nearly an entire year of regular earnings (usually at the highest rate you've earned in your career) but also the payout of your sick leave and vacation balances. Combined, these amounts could very easily place you into a higher tax bracket. However, if you were to delay your retirement into the first few weeks of the new year, your vacation and sick leave payoffs will be combined with your retirement income which is normally **lower** than what you earned as an active employee. Since your income is kept lower by delaying your retirement date, the amount of taxes you would have to pay should also be lower. (Finding a good tax advisor or preparer can also help!)

Q. How much notice do I have to give TCERA before I retire?

A. The retirement laws governing our plan do not allow our office to accept a signed retirement application more than 60 days **before** your actual date of retirement. We encourage members to schedule an appointment with our office about 30 days before you plan to retire. But remember that you are always welcome to schedule an appointment to meet with a Benefit Specialist to discuss your retirement options and benefits. We are here to serve you in planning for your big day!