

KALAMAZOO COUNTY

EMPLOYEES' RETIREMENT SYSTEM



In the Pursuit of Extraordinary Governance...

Summary Annual Report

2016



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2016 SUMMARY ANNUAL REPORT

ABOUT THE KALAMAZOO COUNTY EMPLOYEES' RETIREMENT SYSTEM

This summary annual report is in compliance with Public Act 530 of 2016. The contents came from the Kalamazoo County Employees' Retirement System's (the Plan) Financial Statements and Requirement Supplementary Information, Annual Actuarial Valuation and additional analysis as of December 31, 2016.

The Kalamazoo County Employees' Retirement System was established by the Kalamazoo County Board of Commissioners and is administered by the Kalamazoo County Retirement Investment Committee. This committee consists of citizens who have extensive knowledge and background in the investment and management field, access to the national money managers employed by the Retirement System, and no business or political ties to the County, the Kalamazoo County Road Commission, Kalamazoo County Community Mental Health and Substance Abuse Services (the Authority), or to the Plan.

The Retirement System is controlled by laws established by the State of Michigan. The Kalamazoo County Board of Commissioners approves changes to the Retirement Resolution (Plan Document). For Road Commission employees, the County Road Commission recommends changes to the County Board. For Mental Health employees, the Mental Health Board recommends changes to the County Board.

A Master Trustee, State Street Corporation, Boston, Massachusetts, acts as custodian and as a control and monitoring point for the performance and procedures of the managers. In this way, envisioning an organizational chart, the control over the Retirement System's assets is as follows:

- County Board of Commissioners
- Retirement Investment Committee
- State Street Corporation
- Individual Money Managers

From the County Board of Commissioners' monitoring of procedures to the four managers, performances and control flows from one level to the next.

KALAMAZOO COUNTY EMPLOYEES' RETIREMENT SYSTEM SERVICE PROVIDERS

A service provider is an individual, third-party agent or consultant, or other entity that received direct or indirect compensation for consulting, investment management, brokerage, or custody services related to the system's assets. The System uses the following for professional services:

Clark Hill PLC – Legal Services
Gabriel Roeder Smith – Actuarial Services
Merion Capital – Consulting Services
Rehmann Robson – Auditing Services
State Street Bank – Custodial Services

Based upon the review and recommendations of the Retirement Investment Committee, the Plan's assets are invested with Blackrock Institutional Trust Company, N.A., Dimensional Fund Advisors, INC (DFA), Jennison Associates, LLC, RREEF America REIT II, Inc., and Vanguard.

MEMBERSHIP

An eligible employee becomes a member in the System as of his or her date of regular employment. Participants become 100% vested for benefits after eight years of service. Terminated members vested in the System are eligible for deferred retirement benefits.

The System's membership as of the most recent annual actuarial valuation consisted of the following:

December 31, 2016				
	County	Road Commission	Authority	Total
Retirees and beneficiaries currently receiving benefits	312	36	42	390
Terminated employees entitled to but not yet receiving benefits	143	6	57	206
Vested active participants	313	23	81	417
Nonvested participants	325	18	132	475
Total membership	1,093	83	312	1,488

Retirement Allowances	
Average annual retirement allowance	\$19,298
Total annual retirement allowances being paid	\$6,020,935

BENEFIT STRUCTURE

Regular retirement benefits begin at age 60 with 8 years or more of service for the Authority and the Road Commission employees, as well as the County employees hired before July 1, 2009. Regular retirement benefits begin at age 65 with eight years or more of service for the County employees hired on or after July 1, 2009. Certain County employees are eligible for normal retirement at age 55 with 25 years of service. Members may retire at age 55 with eight years of service for a reduced benefit.

Deferred members of the County hired before October 1, 2009, deferred members of the Authority hired before February 5, 2013, and all deferred members of the Road Commission may elect to receive a lump sum benefit at any time before or after reaching the retirement age. All deferred members may receive annuity benefits at the normal or early retirement age.

Benefits are determined at the member's retirement date based on a formula of the member's service credit, final average compensation, and a percentage factor. Service credit is determined

by the total number of full or part-time (at least 20 hours per week) years and months of employment. Additional service may be credited for Road Commission employees with disability leave and all employees with military. The final average compensation is the average compensation received during the highest 5 consecutive years of the last 10 years of service or all years of service if the employee has less than 10 years of service. The percentage is determined by the participating employers of the System and ranged from 1.7% to 2.5% in 2016 and 2.0% to 2.5% in 2015. Annual benefits are reduced for early retirement or beneficiary benefits. Employees may choose to receive benefits in monthly payments or as a lump sum payment. Lump sum payments for employees hired before October 1, 2009, are calculated using the annual benefit, expected future lifetime, and a discount rate. Lump sum payments are no longer an option available for County employees hired on or after October 1, 2009, and Authority employees hired on or after February 5, 2013. The discount rate shall be the investment return assumption as adopted by the Retirement Investment Committee to be used in the annual actuarial valuation of the System.

ASSETS & LIABILITIES

Total assets as of December 31, 2016 were \$211,947,405 and were comprised mostly of cash and investments. Total liabilities totaled \$4,689,710 resulting in an increase in net position of \$14,356,677 between 2015 and 2016.

Statement of Fiduciary Net Position		
	December 31,	
	2016	2015
Assets		
Cash and cash equivalents	\$6,049,513	\$7,332,364
Investments, at fair value:		
U.S. government securities	24,927,421	24,666,985
U.S. agency securities	4,944,620	5,250,889
Corporate obligations and mortgage-back funds	19,414,859	18,031,340
Mutual funds	87,249,322	80,252,774
Collective trust funds	62,303,010	57,564,082
Real estate pooled separate account	6,090,455	5,689,576
Receivables:		
Sale of investments	532,567	1,092,901
Interest and dividends	334,628	279,204
Employer contributions	26,779	37,645
Other	74,231	10,223
Total Assets	211,947,405	200,207,983
Liabilities		
Benefits payable	809,051	823,597
Accounts payable	97,248	85,000
Purchase of investments	3,783,411	6,398,368
Total liabilities	4,689,710	7,306,965
Net position restricted for pension benefits	\$207,257,695	\$192,901,018

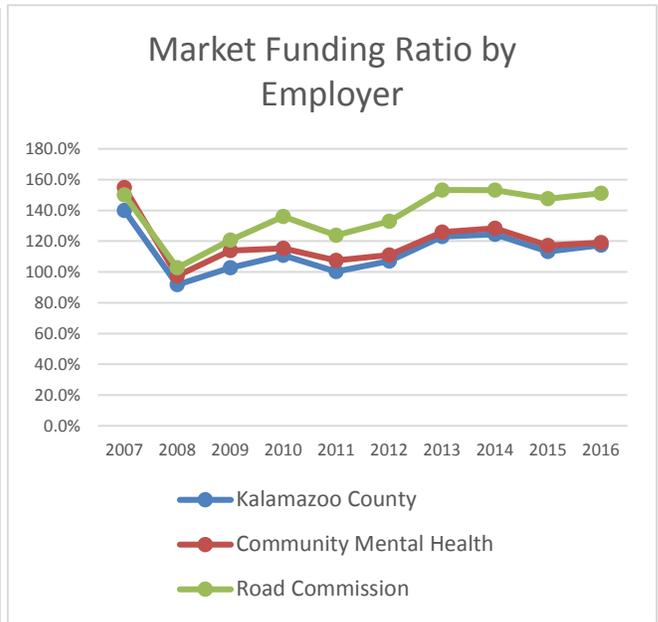
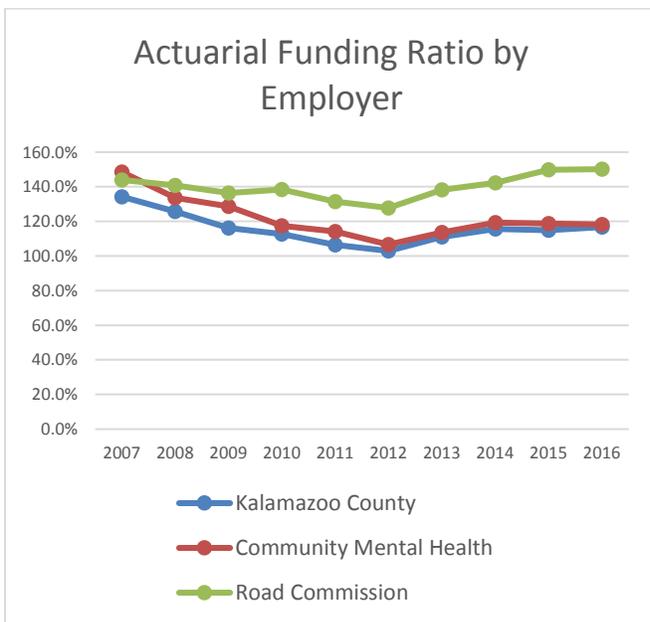
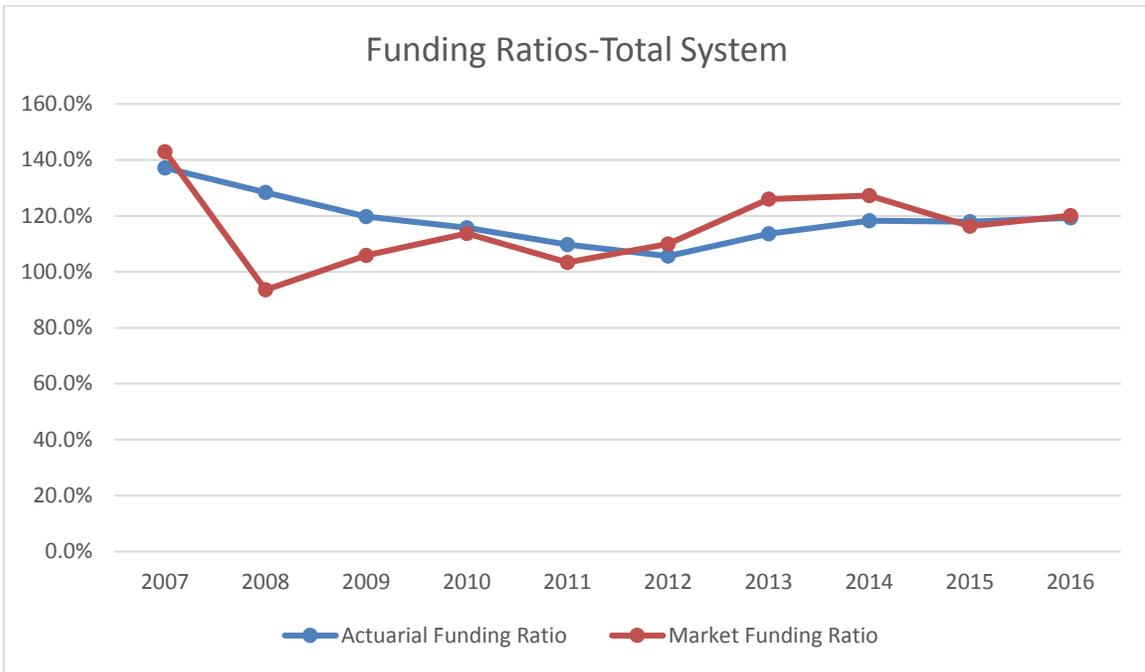
REVENUE AND EXPENDITURES

The reserves needed to finance the plan are accumulated through the collection of employer contributions and earnings on investments. Contributions and net investment income totaled \$24,913,159 for 2016.

Statement of Changes in Fiduciary Net Position		
	For the Year Ending December 31,	
	2016	2015
Additions		
Contributions:		
Employer	1,464,540	1,320,723
Employee	-	4,500
Total contributions	1,464,540	1,325,223
Investment income		
Net appreciation (depreciation) in fair value of investments	18,559,697	(8,062,927)
Income on mutual funds	4,173,139	3,915,316
Interest and dividends	1,311,100	1,268,122
Income on real estate pooled separate account	173,014	259,944
Total investment income (loss)	24,216,950	(2,619,545)
Investment expense	(768,331)	(779,820)
Net investment income (loss)	23,448,619	(3,399,365)
Total additions	24,913,159	(2,074,142)
Deductions		
Benefit payments	10,252,492	9,187,843
Administrative expenses	303,990	345,891
Total Deductions	10,556,482	9,533,734
Change in net position	14,356,677	(11,607,879)
Net position, beginning of year	192,901,018	204,508,897
Net position, end of year	207,257,695	192,901,018

MARKET FUNDED RATIOS & ACTUARIAL FUNDED RATIOS

The actuarial funding ratio uses a five-year smoothing of gains and losses to reduce volatility while the market funding ratio is based on the market value of assets only. The actuarial funding ratio is commonly used by all pension plans to avoid volatility in the System's funding requirements.



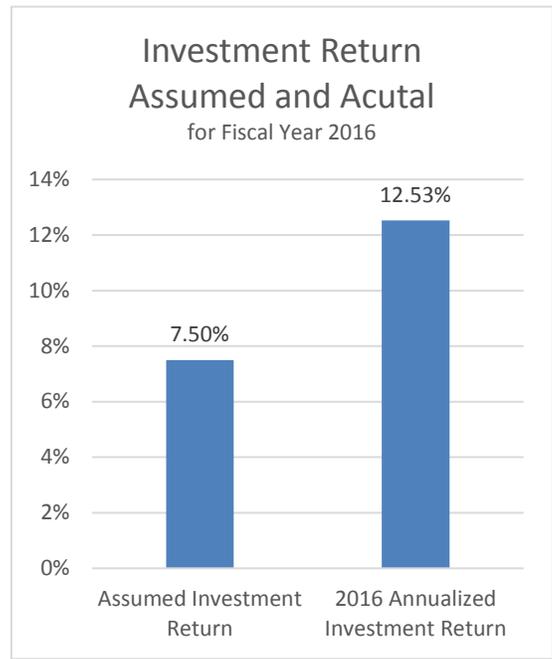
INVESTMENT PHILOSOPHY & INVESTMENT RETURN

The Kalamazoo County Retirement Investment Committee administers all of the System's investments in accordance with the State of Michigan Public Act 307 of 2000, as amended, and the Retirement System's Investment Policy as approved by the County Board of Commissioners. The Retirement Investment Committee's goal is to find a balance or mix between the extremes, i.e., a philosophy that would prudently meet the objectives of properly funding present and future payments to participants. The present policy is seventy (70%) percent of Plan assets at market can be invested in corporate equities and five (5%) percent in real estate, which are the maximums allowed by State law.

The contribution rates are determined by an actuary based in part on an assumed investment return each year. When investments exceed the assumed rates of return, as they did in 2016, this results in a gain for the system. The actual rate of investment return in FY 2016 was 12.53% which is greater than the assumed rate of return.

Actual investment performance is reviewed and reported quarterly to the Retirement Investment Committee and is summarized as follows:

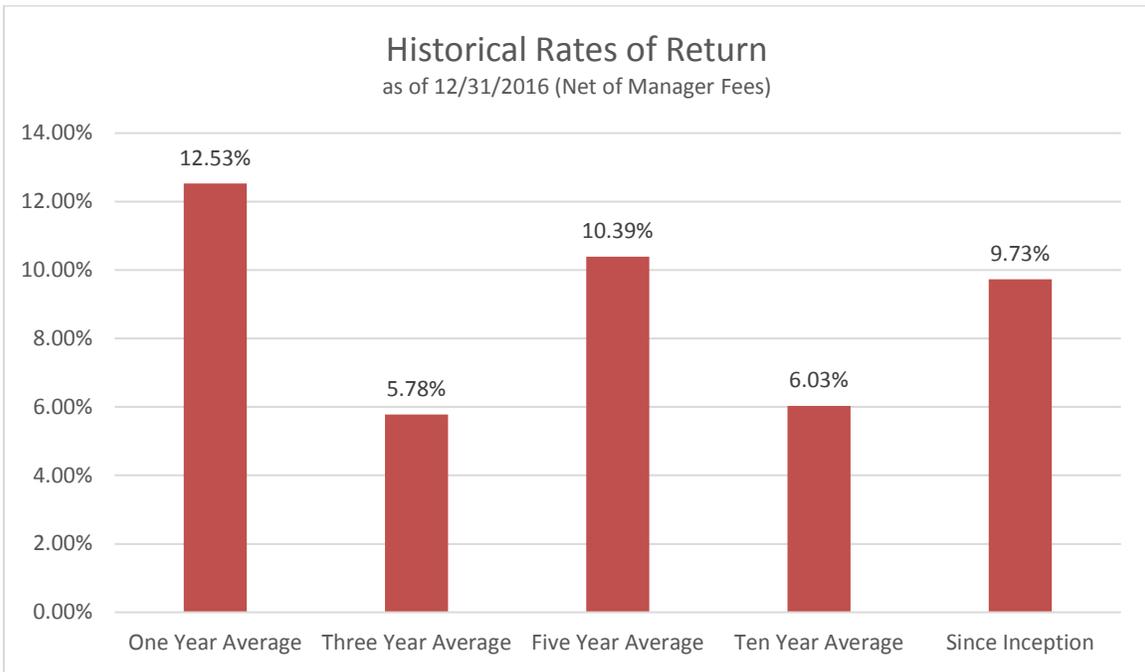
The market value of portfolio assets increased from \$202.4 million to \$219.6 million during 2016, an increase of \$17.2 million or 8.5%. The portfolio weighted average return for the quarter, net of manager fees, was 3.09%. The 1-year annualized net return was 12.53%, and the return since April 1988, net of manager fees, through the end of the quarter has been 9.73%.



Equities comprised 70.0% of the County portfolio at the end of the quarter. The equity portion of the County portfolio returned 16.19% year-on-year. Fixed income comprised 24.4% of the County portfolio at the end of the year and total fixed income returned 2.98%. At the end of the quarter, real estate investments were 4.8% of the portfolio and the one year return on real estate was 9.76%.

The portfolio closed the year with 70.0% in equities, 24.4% in fixed income, 4.8% in real estate, and 0.8% in cash.

The inflation-adjusted, or real return, for the quarter ending 12/31/2016 was 3.09% as the inflation rate for the quarter was 0.00%. With a year-on-year inflation rate of 2.07%, the one year real return was 10.46%. Since April 1988, the return on the portfolio, net of manager fees, has been 9.73% nominal and 7.16% real.

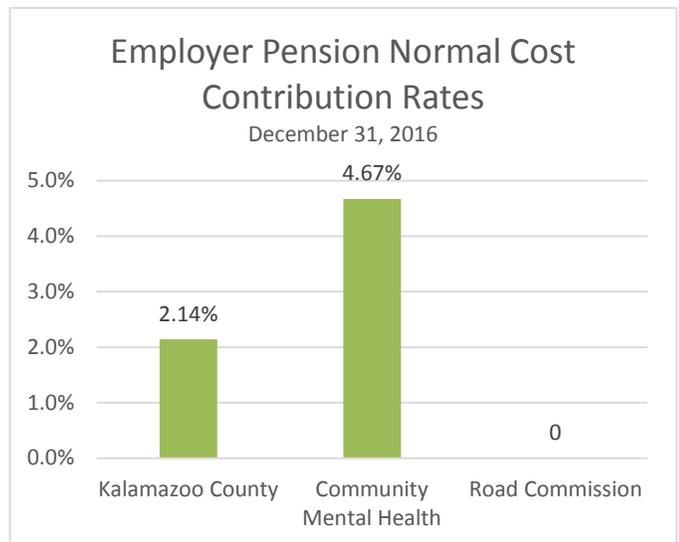


MEMBER AND EMPLOYER CONTRIBUTIONS

It is required by the Michigan Constitution to fund financial benefits arising on account of service rendered in the fiscal year. Contributions made to cover the normal cost satisfy this requirement. The actuary calculates the total annual contribution to the Retirement System as the normal cost plus a contribution towards unfunded actuarial accrued liability. The Kalamazoo County Employees' Retirement System currently has an overfunded liability.

Normal Cost is the annual cost assigned, under the actuarial funding method, to current and subsequent plan years. Sometimes referred to as "current service cost." This is set using the assumed rate of investment return in addition to other actuarial assumptions.

The Kalamazoo County Employees' Retirement System is supported by contributions from the sponsoring entities and by the investment income earned on System assets. Employees do not contribute to the plan. The employer's contribution rates are determined annually by the system's actuary and are determined by the benefit provisions of the System. The employer's contribution is the remainder needed to meet the financial objective.



Employer Pension Contributions		
Computed Normal Cost of benefits expressed as a percentage of valuation payroll		<u>2016</u>
	County	2.14%
	Road commission Authority	4.67% 0.00%
UAAL contribution rate expressed as a percentage of covered payroll		<u>2016</u>
	County	(73.8%)
	Road commission Authority	(246.0%) (49.5%)
Covered Payroll		<u>2016</u>
	County	\$29,427,402
	Road commission Authority	\$ 2,459,213 \$11,131,696

2016 PENSION PLAN EXPENDITURES

Pension Plan Expenses for the Year Ended December 31, 2016	
Administrative and Other Expenses	
Actuary	\$77,252
Insurance	3,703
Audit	19,555
Consulting Fees	64,096
Legal Fees	17,684
Due Diligence/Travel	6,580
Miscellaneous Administration	115,120
Total Administrative Expenses	<u>303,990</u>
Investment Expenses	
Custody Fees	151,841
Advisor Fees	616,490
Total Investment Expenses	<u>768,331</u>
Benefits Paid to Members	
Retirement Benefits	10,252,492
Total Benefits Paid to Members	<u>10,252,492</u>
Total 2016 Pension Plan Expenditures	<u><u>\$11,324,813</u></u>

2016 BUDGET FOR PENSION PLAN ADMINISTRATIVE EXPENDITURES

Budget for Pension Plan Expenses for the Year Ended December 31, 2016	
Administrative and Other Expenses	\$260,000
Investment Expenses	
Custody Fees	175,000
Advisor Fees	640,000
Total Investment Expenses	<u>815,000</u>
Total 2016 Pension Plan Budget	<u><u>\$1,075,000</u></u>

ACTUARIAL ASSUMPTIONS

The actuarial assumptions used in 2016 were based upon the results of an Experience Study for the County of Kalamazoo Employees' Retirement System covering the period January 1, 2009 through December 31, 2013. A report dated February 20, 2015 presented the results of this Experience Study. The actuarial assumptions represent estimates of future experience. Unless otherwise noted, the assumptions were first used with the actuarial valuation date of December 31, 2014.

Actuarial Assumptions for the Year Ending December 31, 2016			
Valuation Date	12/31/2016		
Actuarial Cost Method	Entry-age normal		
Amortization Method	Level percentage of payroll, open period		
Remaining Amortization Period	10 years		
Asset Valuation Method	Market value with 5-year smoothing		
Inflation Rate	3.5%		
Projected Salary Increases (including inflation)		<u>2016</u>	<u>2015</u>
	County	3.50% to 5.50%	3.50% to 7.50%
	Road commission	3.50% to 7.23%	3.50% to 7.20%
	Authority	4.00% to 5.50%	3.50% to 5.50%
Investment Rate of Return	7.5% net of investment expenses		
Retirement Age	Experience-based table of rates that are specific to the type of eligibility condition. Last updated for the 2014 valuation pursuant to an experience study of the period 2009 -2013.		
Mortality	RP-2000 mortality combined healthy tables, projected 20 years with U.S. Projection Scale BB.		



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FINANCE DEPARTMENT

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This report can be found online at
www.kalcounty.com/finance/2016KCERSSummaryAnnualReport