May, 2011

POLICE AND FIREFIGHTERS PENSION BOARD
REGULAR BOARD MEETING
WEDNESDAY, MAY 4, 2011, 12:30 P.M.

Present
Michael Dew, Chair
Ken Rudominer, Vice Chair
Richard Fortunato, Secretary
J. Scott Bayne, Trustee
Mark Burnam, Trustee
Dennis Hole, Trustee
Alison Bieler, Cypen & Cypen, Board Attorney
Lynn Wenguer, Administrator

Absent
Jim Naugle, Trustee

Also Present
Amanda Cintron, Assistant Administrator
Kevin Schmid, CapTrust
Jonathan Woodruff, CapTrust
Randall L. Stanley, Stanley, Holcombe & Associates
Gloria LeClaire, Controller
Fred Nesbitt, Director of Media Relations
Gregg Gurdak, President, Retirees' Association
Linda Soloman-Duffey, Secretary, Retirees' Association
Frank Colleran
Henry Sledge
Jack Lundstrom
Jim Annin
Jack Cann
Rick Schulze
Mike Clarke
Walter Courtney
John Stuber
Robert Root
George Farrell, Jr.
Bill Paton
Pete Loftus
Ron & Donna Pritchard
Jim Ingersoll
John H. Yancey
David McArdle
Barbara Hartmann, Recording Secretary, Prototype, Inc.

Pursuant to authority of Ordinance C-00-34, Article II, this regular meeting of the Police & Firefighters' Pension Board convened at 12:30 P.M., Wednesday, May 4, 2011, in the Pension Board Conference Room, 888 S. Andrews Avenue, Suite 202, Ft. Lauderdale, Florida 33316.

Communications to City Commission

The actuary has verified that the modifications made to the DROP plan have reduced the plan's unfunded actuarial liability. The Board requests that Chair Dew make a short verbal presentation of the actuarial results to the City Commission.

Chair Dew called the meeting to order at 12:30 p.m.

MINUTES: Regular Meeting

Motion made by Vice Chair Rudominer, seconded by Mr. Hole, to waive the reading of the minutes from April 13, 2011.

Mr. Hole noted the following corrections:
P.4, paragraph 4: correct "as issues" to "on issues;"
P.6, paragraph 2: correct "hired" to "invested with;"
P.11, paragraph 5: correct "to set up service" with "to present to the Board."

Mr. Bayne noted the following corrections:
P.8, paragraph 2: omit "administration;"
P.11, paragraph 4: question was posed by Mr. Bayne rather than Mr. Burnam;
P.12, paragraph 8: should state "Ms. Wenguer explained that firefighters receive some assignment pays and upgrade pays that are pensionable earnings."

Mr. Hole requested that the minutes reflect that he, Mr. Bayne, Vice Chair Rudominer, Ms. Wenguer, and Ms. Cintron attended an educational conference.

In a voice vote, the motion passed unanimously.

Chair Dew ceded the chair to Vice Chair Rudominer for the approval of benefits, as he is on the Agenda as a DROP retiree.

BENEFITS:

Motion made by Mr. Bayne, seconded by Mr. Fortunato, to take the Police Department benefits individually.

Police Department:
DROP Retiree: Marc A. DeCarlo
Michael J. Dew

Motion made by Mr. Burnam, seconded by Mr. Fortunato, to approve benefits for Marc A. DeCarlo as stated. In a voice vote, the motion passed unanimously.

Motion made by Mr. Burnam, seconded by Mr. Hole, to approve benefits for Michael J. Dew. In a roll call vote, the motion passed 5-0. [Chair Dew abstained. A memorandum of voting conflict was submitted.]

New Beneficiary: Marcella Madeline

Motion made by Mr. Burnam, seconded by Mr. Fortunato, to approve the beneficiary of Marcella Madeline. In a voice vote, the motion passed unanimously.

Lump Sum Refund: Richard J. Lemack
Max S. Weitzner

Motion made by Mr. Burnam, seconded by Mr. Fortunato, to request the lump sum refund for Richard J. Lemack. In a voice vote, the motion passed unanimously.

Motion made by Mr. Burnam, seconded by Mr. Fortunato, to request the lump sum refund for Max S. Weitzner. In a voice vote, the motion passed unanimously.

Fire Department:
New Retiree (Term. Of DROP): Karl W. Wright

DROP Retiree: Timothy J. Habig

Lump Sum Refund: Justin K. Medlin

Motion made by Mr. Burnam, seconded by Mr. Hole, to approve the Fire Department retirements and refunds. In a voice vote, the motion passed unanimously.

Vice Chair Rudominer returned the chair to Chair Dew at this time.

BILLS:

NorthPointe:	$84,060.88
Sawgrass Asset Mgmt.:	$40,311.00
Systematic	$33,572.49
The Northern Trust Company:	$29,370.44
InTech:	$21,376.28
CapTrust:	$18,750.00
Marcum:	$14,512.50

Motion made by Vice Chair Rudominer, seconded by Mr. Burnam, for the payment of the bills as documented.

Mr. Hole noted that some bills were dated March but stamped in April, and requested clarification that bills are stamped when they are received. Ms. Wenguer confirmed that this is the policy.

In a voice vote, the motion passed unanimously.

INPUT FROM ACTIVE & RETIRED POLICE OFFICERS & FIREFIGHTERS:

Mr. Gurdak read a letter into the record in response to Chair Dew's statement at the April 13, 2011 meeting. [A copy of the letter is attached to these minutes.]

Chair Dew thanked Mr. Gurdak for his response. Chair Dew said the purpose of his letter was to address questions from the retirees. In addition his statement was not an attempt to criticize the Retirees' Association, but was intended to engage the Association and get a response. He felt the statement had achieved this goal, and said the Board looked forward to working closely with the Association and making sure the benefits they have all fought for are insured for the future.

2011 ACTUARIAL REPORT:
Stanley, Holcombe & Associates Randall Stanley

Mr. Stanley provided the Board members with a copy of the 2011 Actuarial Report. He referred the members to the cover letter, noting that the calculation of rate of return on the assets of the trust at market value for 2010 was 11.8%. He explained that they use smoothing on the asset values in order to dampen the volatility of City contribution requirements; because of this, the rate of return on the smoothed value of assets was 6.3%. He reminded the Board that because of current economic conditions, losses still have to be made up from past years, which is the reason for the lower rate of return.

Chair Dew asked why the actuarial rate of return is different from the auditors' rate of return. Mr. Stanley explained that he took the beginning and ending market values less the investment return, divided by two; this is then divided into the rate of return on the market value basis. He did not know how the auditors made their calculations.

Chair Dew noted that the difference between 12.4% and 11.8% is significant. Mr. Stanley suggested that investment expenses could be a reason for the disparity, as this cost is roughly 40 basis points. He reiterated that he did not know how the auditors made this calculation. Chair Dew said he would like a clarification on this issue. Mr. Stanley agreed to look into this.

He returned to the cover letter, noting that there was a net experience gain of roughly $854,000 in 2010. While this is not a major issue, he noted that it is progress.

Chair Dew requested clarification of the “hole” the fund was coming out of, and asked if this meant the investment losses from 2008. Mr. Stanley referred the Board to p.1, Item B, which shows the smoothed asset value of January 1, 2010 at $452 million when the actual market was $405 million. The actuary used an asset value of approximately $47 million more than market value. In January 1, 2011, the gap has narrowed, although it is still roughly $27 million. He characterized this as making progress in getting out of the hole, but emphasized that it will take time.

Mr. Stanley advised that another hole the fund has been in is gain-sharing for the cost of living adjustment (COLA). He recalled that up to four years ago, the COLA provision in the Ordinance was thought to be eliminated. He referred the members to pp.41-44, stating that by December 31, 2007 there was a cumulative loss of $13 million; in 2008, the loss increased to $81 million; in 2009, the loss increased to $114 million; and in 2010, the loss came to $122 million. Mr. Stanley explained that this means there cannot be a gain-sharing COLA transfer until there is no longer a cumulative loss. To overcome this cumulative loss, there must be a rate of return of roughly 20% over and above the loss.

Chair Dew asked why the loss of 2008 was increased further with an additional loss in 2010. Vice Chair Rudominer requested an explanation of cumulative loss or gain. Mr. Stanley referred the members to p.44, which shows there was an expected unfunded actuarial liability at the end of 2009; at the end of 2010, the calculated expected unfunded liability was $70 million, with an actual unfunded liability of $192 million. This resulted in a net loss of $122 million.

Chair Dew said if the performance was better in 2010, the loss should be less. He pointed out that the unfunded liability was increased by $5 million, but the increase in the experienced loss was $8 million, which did not make sense.

Mr. Stanley said he was attempting to keep a bridge in place under the premise that there may need to be some gain-sharing COLAs granted in the future, although currently this is not possible. He said a 20% rate of return is needed over the actuarial investment return assumptions in order to overcome the loss. He noted that cumulative expense positions are universal.

Mr. Ingersoll asked when the smoothing period changed from three years to five years. Mr. Stanley said he believed this was recommended nine years ago, when his firm was hired. Smoothing of asset value is very popular when markets are in a downturn, but less so when they are moving back up. In 2002, when the markets began going down, the smoothed value declined less dramatically. As 2008 approached, however, the markets began taking off and increased the smoothed value as well, although this increase was not as dramatic as the overall market increase. When the markets began declining again, the smoothed value did not decline as much, which he concluded was exactly what smoothed asset value is supposed to do.

Mr. Stanley called the Board’s attention to the $823 million funding target, which is the present value of all projected benefits: if the trust had this amount in it on January 1, 2011, theoretically they would never need another contribution from the City, State, or any active members. The actual accrued liability is $674 million. If this amount was deducted from the actuarial value of assets, the $192 million actuarial unfunded liability would remain. This becomes a component of the City’s funding requirement and is amortized over approximately 20 years.

He explained that these components show the fund had a $482 million asset value and a $674 million accrued liability, which means the funded percentage of $111 million is roughly 71.5%. Mr. Stanley noted that this percentage is moving in the right direction for the fund. Until 2001, the funded percentage was higher than the current 71.5%; it then began moving downward beginning in 2002, and has been in the range of roughly 70% since that time. The target for the trust is 80% funded; if this is not possible, the goal is for improvement, which is presently occurring.

Vice Chair Rudominer asked why the goal for the trust is 80% funded rather than 100%. Mr. Stanley said if funding is at 100%, the trust would be considered overfunded, as the expectation is to amortize unfunded liabilities

over a period of roughly 20 years. As long as amortizable liabilities remain, a plan should not be 100% funded. He added that 80% is a nationwide standard: if funding is above 80%, a plan is considered overfunded.

Mr. Stanley advised that in the event of robust overfunding, some of the amortization charges would disappear and the City's contribution would decrease. While this also seems to be good news, it would require an explanation of how it happened.

Mr. Hole asked if the Board needed to revisit any assumptions, such as a disparity in the DROP, to determine how they would affect the plan's numbers. Mr. Stanley referred to p.5, stating that elements such as retirements and DROPs reduced the unfunded liability by roughly $3.3 million. He noted that there were 21 retirements/DROP entries in 2010 against an expectation of 40: in a poor economic environment, participants consistently postpone retirement, which produces a favorable result for the trust. He added that because there is less turnover from workers leaving, this can produce a loss to the trust. For the plan, fewer retirements resulted in a gain of $3.3 million while fewer turnovers resulted in a loss of $1.6 million.

Chair Dew said the last collective bargaining contract for Police Officers and Firefighters allowed participants to work two years longer before they were allowed to enter the DROP program. The general opinion is that this will continue, as many members were previously forced to retire sooner than they wanted to. Mr. Stanley agreed that this was a smart change, and pointed out that if several years result in consistent gains of $3.3 million, it would be a very positive result for the trust.

Vice Chair Rudominer remarked that this seems to be confirmation that the recent modifications to the DROP have reduced the actuarial unfunded liability. Mr. Stanley agreed with this, although he advised to keep the difficult economic environment in mind as well. He suggested that the gains continue to be quantified year by year in order to lend more statistical credibility to the data. If at a later date, the results have been totally consistent, the retirement assumption will need to be modified to reflect that a percentage of members will wait longer than previously expected before retiring. He cautioned, however, that one year's results are not sufficient to cause this modification.

Mr. Stanley moved on to a summary of the actuarial basis. Significant assumptions are that the investment return is expected to average 7.75% annually; embedded in this is an annual inflation assumption of 3.75%. The inflation is part of both the investment return and the salary increase assumptions. For salary increases, there is also a service-based probability ranging from 7.5% annually for early employment to 0.5% annually for participants with more than 26 years. The 1994 group annuity mortality table is being used. He noted that mortality is not a particularly important assumption for a retirement system: the system is instead dominated by the investment returns. The 1994 table is still used, although a more recent table is now available, because the actuary is trying to wait until a period of primarily good news occurs before making this change.

Mr. Hole asked if Mr. Stanley could estimate how the liabilities would change if new percentage tables were used. Mr. Stanley said the change would likely be in low double digits.

Chair Dew noted that of expected City contributions, covered payroll is 49% and total payroll 44%. He asked if this difference was due to the equation with the DROP. Mr. Stanley said this will be revisited and replacement pages may be supplied, as he and Ms. Wenguer had discussed this issue. He said there is consideration of including payroll for DROP in the payroll for active members, due to the argument that without DROP, these participants would be retired and there would be more active members. Chair Dew requested that this be included in the narrative with an explanation, so it is clearly spelled out if City Commissioners read the narrative.

Mr. Stanley said they had assumed that the 2009 payroll for active participants went up by 6%; then, when the payroll for DROP participants was received, they had had to determine whether or not this payroll would include members who were in DROP at some point during the year but were not still in DROP by the end of the year. The best estimate for projected payroll in 2010 had been that this would increase by 3.75%. With no reason to change this, it was expected that the same calculation would be used in 2011.

He continued that the State Division of Retirement is now taking the position that the minimum City contribution must be the calculated contribution percentage applied to the actual payroll. This is in contrast to funding the actuarially determined dollar amount, which was done in the past. Mr. Stanley said he believed the new calculation

is flawed, because when payroll decreases in the current environment, it is not a good time to cut contributions. He said his recommendation was that the calculated contribution percentage be applied as a minimum, and advised that the State is already beginning to enforce this means of calculating the contribution.

He pointed out that the State says if a plan is permitted to continue separating 175 and 185 monies, which has been done since 1999, costs must be separated as well. This means assets must be allocated into two pools, one for Police and one for Firefighters, which has not previously been done in this system. Mr. Stanley said the alternative would be to combine 175 and 185 monies, which would be very difficult. Once the liabilities are separately calculated, the assets are split and subtracted, which results in separate unfunded liabilities of $112 million for Police and $80 million for Firefighters. The present value of future benefits is then calculated, and the City contribution is determined separately for Police and Firefighters. Of the $30 million total, the Police contribution is $17 million and the Firefighters contribution is $13 million. He advised that it is not yet clear that this exercise can be repeated annually as if the prior year did not occur; the alternative to this would be splitting the assets and then maintaining the trust accounting separately between Police and Firefighters assets.

He concluded that this requirement results in extra work without significant extra value. Chair Dew asked if the current legislation dealing with premium taxes could affect this. Mr. Stanley said it would have an effect.

Gloria LeClaire, Controller for the Finance Department, said she had believed a decision was made to start 2012 with the fiscal year rather than the calendar year. Chair Dew confirmed this. Mr. Stanley explained that the report was for the year beginning October 1, 2011, and another evaluation would be done at that date for fiscal 2012. He noted that there is an interest charge included in the contribution requirement because calculations were done on January 1, but contributions did not come in until the fiscal year began months later.

Ms. Wenguer requested clarification that the City's contribution would be made on October 15, 2011, which is part of the new fiscal year; this would mean there was no contribution for the nine months prior to this. Mr. Stanley said he felt the State would not have a problem with this. He said the current evaluation report, made on January 1, 2011, is for the fiscal year beginning October 1, 2011 and ending on September 30, 2012.

He noted that total interest is over $2 million, which is money that the trust charges the City for not making their contribution on January 1, 2011. If the City wants to lessen this, there would need to be a scheme by which they estimate contributions and make them earlier.

Ms. LeClaire said there is already a 2011 report that states what the City will need to pay in October, which is $30.6 million. Chair Dew observed that the City makes their contribution relatively early in the fiscal year, on October 15, which would reduce their interest; Mr. Stanley advised that they would need to find a way to get the money into the trust earlier in order to see a reduction in interest. The calculation date is in January, while the deposit date is in October. Ms. Wenguer explained that making the payment earlier in the year would mean it came out of the 2010-11 budget rather than the 2011-12 budget.

Mr. Stanley stated that his firm has signed a definitive contract to merge into Nyhart, as discussed at the March 2011 meeting. They plan to close on May 31, 2011, effective June 1st. Ms. Bieler said Nyhart has accepted the assignment of the contract and has agreed to assume all of the responsibilities after closing.

Ms. Wenguer noted that there are numerical errors in the report. Mr. Stanley said these are associated with the DROP payroll, as they had tried to rush these figures. Chair Dew said approval would be deferred until the next meeting for this reason.

Motion made by Mr. Bayne, seconded by Mr. Fortunato, to approve the assignment of the actuary contract to Nyhart. In a voice vote, the motion passed unanimously.

The following Item was taken out of order on the Agenda.

Retiree Frank Colleran

Chair Dew recalled that the Board had discussed in April that Mr. Cypen would not be present to further discuss the issue at today's meeting. Ms. Wenguer confirmed that she had notified Mr. Colleran's attorney of this.

Mr. Colleran stated that this issue had been going on for nearly three years, and asked if it was possible to get a guarantee that the information from Mr. Stanley's firm would be available at next month's meeting, so he and others could plan to attend the next meeting with attorneys present and resolve the issue. Chair Dew said he did not know if it was possible to make such a guarantee. He explained that the 2011 Actuarial Report was a priority according to State law.

He asked Mr. Stanley how long he felt it would take to come up with the information. Mr. Stanley said he hoped it would be prior to next month's meeting. Chair Dew asked if July would be a more appropriate date, noting that several individuals with a stake in the issue had made plans to attend today's meeting to hear resolution of the issue. He added that they would also need to ensure that Mr. Cypen would be available for the discussion. He stated that resolution of the issue would come down to the actuarial calculation and a legal opinion, as it is very confusing to himself and the other Trustees.

Chair Dew concluded that the Board would find out what information Mr. Stanley had come up with and would speak to Mr. Cypen; then Ms. Wenguer would notify Mr. Colleran with a date on which he and the other affected individuals could plan to attend a meeting and hear resolution. He advised that he could not definitively state that all information would be available at the next meeting, as he could not be sure Mr. Stanley would have the information at that time.

Mr. Stanley suggested that they set a target date of two weeks prior to the next meeting for him to contact Ms. Wenguer and inform her whether or not the figures would be available in time for the meeting. This information would then be passed on to Mr. Colleran. It was determined that Mr. Stanley would contact Ms. Wenguer by the end of the business day on May 25.

Mr. Colleran said he would like to see the information available for dispersal to those affected at the June meeting. The issue could then be scheduled for further discussion, and hopefully for resolution, at the July meeting. Chair Dew explained that he could not firmly schedule this discussion for the July meeting at this time, as there is an informal disability hearing coming up that also has to be scheduled. This hearing would take precedence due to its time-sensitive nature.

Ms. Soloman-Duffey asked if there is a list of how many retirees are affected. Ms. Wenguer said there is not a complete list of those affected by this issue.

Mr. Colleran asked if the formula given to Mr. Stanley by attorney Alan Eichenbaum would be used. Mr. Stanley said to his recollection, the formula provided by Mr. Eichenbaum's earlier correspondence "would lead [him] to not agree with it." He reiterated that his firm was working on retroactivity and would review these communications with Mr. Eichenbaum as part of the process.

Mr. Colleran said his understanding was that Mr. Stanley had agreed to use a specific percentage as stated by Mr. Eichenbaum at the last meeting at which they were both present. He said the formula had been included in correspondence to Mr. Stanley from Mr. Eichenbaum, and recalled that Mr. Cypen had agreed that this formula would be used. Mr. Stanley said he did not recall Mr. Cypen making this comment about a particular formula.

Vice Chair Rudominer said the Board had tasked Mr. Stanley with coming up with the appropriate calculation; this would be the information that is needed by May 25. Chair Dew asked Mr. Stanley to meet with Mr. Cypen and Ms. Wenguer to refer to the historical data within the next day or two to settle this issue; once it has been clarified, he asked that the information be sent to Ms. Wenguer, who would send the information on to Mr. Colleran.

Ron Pritchard, Fire Department retiree, asked to be included in any emails distributed on this issue. He explained that he had set up an email tree for distribution to the other similarly positioned retirees.

John Yancey, Fire Department retiree, said he had not heard any discussion about loads or costs, either fiscally or annually, and he would like to know a figure of what is being paid to money managers over a year. It was determined that this was $1.4 million.

CAPTRUST: Kevin Schmid, Jonathan Woodruff

Quarterly Investment Review

Mr. Schmid distributed the Quarterly Performance Review to the Board members. He referred them to the capital markets review, stating that very little was gained from short- to intermediate-term fixed income in the first quarter; the aggregate bond index was up only 42 basis points for the quarter. The equity markets were up 5.9% for the quarter, primarily driven by the energy and industrial sectors. Most other sectors returned within the 3%-4% range according to the Standard & Poor 500. This was well behind the overall market performance.

Mid and small cap continued to outperform larger caps, with mid cap up 7.6% and small cap up 7.9% for the quarter. Looking at equities over the three-, five-, and ten-year ranges, Mr. Schmid advised that these performances are projected better than they have been in the recent past, up 3.3% annualized over the last ten years. Although this is an improvement, he noted that there is still a long way to go in order to meet the required 7.75%. The plan is earning 7.42% annualized since the inception of CapTrust's data, which dates back to the end of the third quarter in 1995.

Mr. Schmid said over the last three years in particular, the fund has had a higher return than its policy benchmark, but with a lower risk factor as measured by standard deviation. The plan's managers have achieved returns that are in line with or ahead of their benchmarks, and in most cases have done so with less risk.

He continued that the majority of managers outperformed their benchmarks, particularly on the large cap side. InTech was up 6.3% for the quarter and 40 basis points ahead of the S&P 500. Sawgrass outperformed during the first quarter, up 6.8% against a benchmark of 6.02%. They are still lagging over a three-year period; Mr. Schmid recalled that this was discussed at a previous meeting, and it was noted that the current market does not favor their style.

Vice Chair Rudominer asked if the market came to Sawgrass or if they changed their style. Mr. Schmid said according to Sawgrass, the markets came to them: the periods in which they do not perform well are when greater market risk results in better performance.

Chair Dew noted that while Sawgrass has had recent opportunities, they have lost 200 basis points during the three-year period. He asked if this warranted placing Sawgrass on a watch list. Mr. Woodruff said 200 basis points over a three-year period would not flag them for a watch, particularly within a market that experienced a 30% swing within one year. He pointed out that a manager like Sawgrass could make up 60 basis points within one day.

Mr. Schmid added that they are generally more concerned when managers underperform during periods in which they are expected to outperform. He reiterated that Sawgrass is in a type of market in which they do not historically perform well; CapTrust would not become concerned unless they weather this part of the cycle and then do not rebound in a meaningful way. He concluded that they do not recommend terminating managers for performance reasons only, unless that performance is symptomatic of a change in management philosophy or is out of character with historical performance.

Chair Dew asked how long a poor performance will be tolerated by a manager until the determination is made to cut losses. Mr. Schmid said he expected this to be a critical year for Sawgrass, as they should continue to improve.

Mr. Woodruff said Sawgrass is part of a large bucket of managers that show growth at a reasonable price: this group of managers focuses on high quality and have had difficulty competing with lower-quality small cap stocks, which have dominated the performance of the index. In the first quarter, however, there have been reports that this trend is starting to turn, and quality is once again beginning to matter more, although the lower-quality rally had lasted longer than anticipated.

He continued that Systematic finished in line with their benchmark for the quarter, at 6.54% against 6.46%. On the small cap side, Lee Munder lagged behind for the quarter, at 4.8% against a benchmark of 6.6%, although Mr. Schmid pointed out that over one year, they added 40 to 50 basis points and performed very well over a three-year period. He noted that although a decision has already been made on NorthPointe, they are up for the quarter, at 8.7% against 9.2%. While their one-year figures show a rebound of 37%, their three-year numbers remain behind the benchmark.

Among international managers, Artio remains under watch. They were up 2.1% against a benchmark of 3.4% for the quarter. For the year, they are in line at 10.2% against 10.4%. Mr. Schmid advised that they have solid emerging market exposure, although emerging markets lagged behind developed markets in the first quarter. He concluded that it was a disappointing quarter for Artio. Conversely, Thornburg outperformed their benchmark by 4.2% against 3.36%. Both these managers were underweight in exposure to Japan.

On the fixed income side, Agincourt continues to add consistent value against their benchmark, and were up 73 basis points against a benchmark of 42 for the year. Mr. Schmid said Agincourt is moving from shorter-term securities to more intermediate-term in an effort to get more income into the portfolio.

He recalled that real estate had been discussed at the April meeting when American Realty had made a presentation to the Board. He has also recently met with Prudential, which is up 5.5% over the last quarter. Mr. Schmid concluded that K2 was up 1.72% for the quarter. They had reduced their risk in the first quarter by focusing on stocks rather than on broad-based markets exposure.

He referred the Board to tab 8, which certifies that the plan is in compliance with its investment policy statement and all applicable laws. CapTrust has noted two minor exceptions to this. Mr. Schmid explained that managers cannot have exposure to securities that are on the State Board of Administration (SBA) watch list for having business ties to questionable nations. Agincourt has notified CapTrust that as of March 31, 2011, they held two securities in a company that was on this list. As part of the compliance process, these two bonds were ultimately sold. As part of the investment policy statement, Agincourt was supposed to be out of these securities as of September 30, 2010.

He advised that the first bond was sold on October 6, 2010, resulting in a gain of $6856; the second was sold on April 26 and suffered a market value loss of $13,786. Neither Agincourt nor Asset Consulting Group caught this mistake.

Ms. Bieler explained that a quarterly list, published by the State Board that administers the Florida Retirement System, includes companies from which public pension funds are prohibited from investing. In this case, there was an error that resulted in the ownership of a prohibited bond. The law directs all boards to divest of these securities by a specific date. As this case occurred when one company was acquired by another, Ms. Bieler said there was apparent confusion regarding when the acquiring firm was on the SBA list; there is a need to determine when they got on the list, as the Board is required to dispose of prohibited assets within a reasonable period of time. If the asset was retained and then sold after September 20, the manager is responsible to the Board for any losses. She concluded that it is not yet clear whether or not the firm was on the list at that time.

Mr. Schmid said according to the quarterly update, the acquiring company has been on the list since 2007; however, it is not clear whether or not they inherited this status from the company they acquired. From a market value standpoint, the bond suffered a loss of $13,786, on which $7400 was earned in interest. He calculated this as a net loss of $6370.

Ms. Bieler continued that a letter will be sent to the company, by the Plan Administrator, advising them of their error. The plan does not face any penalties for the manager's actions. She pointed out that the issue was rectified as soon as CapTrust became aware of it.

Mr. Schmid concluded that hopefully there will be no other exceptions of this nature in the future.

Monthly Progress Report

He referred the Board members to the Progress Report, noting that the two new fixed income managers, Boyd Watterson and Atlanta Capital, are now operating. With regard to small cap, Franklin Portfolio Advisors' legal team has just sent over the final agreement. He expressed some frustration that the process of bringing in Franklin Portfolio Investors has taken longer than originally intended.

Ms. Bieler observed that some of the larger companies, with large in-house legal teams, can be more difficult to deal with. Chair Dew agreed that when a manager presents to the Board, there should be contingencies made that

ensure contracts will be facilitated in a timely manner, such as within one month. Mr. Schmid pointed out that this message was conveyed to both Franklin Portfolio Investors and Eagle Asset Management up front.

Ms. Bieler advised in the case of Franklin, the issue creating the delay was soft dollar research: they wanted to have trades at whatever price they deemed appropriate in exchange for having the benefit of the research of other firms and brokers. She stated that her understanding was the Board had a policy of best execution and would not be willing to pay for research dollars. There had been some back-and-forth on this issue that created the delay.

Vice Chair Rudominer asked if this was something a presenter would know. Ms. Bieler said typically a consultant will not bring a manager to a fund if that manager operates within a set of parameters that would not agree with the Board's. Mr. Schmid added that in most cases, when pressed, a manager will make the changes requested by a fund's attorney. This was ultimately the case with Franklin.

He recalled that the Board's original decision was to split the mandate between Franklin and Eagle, and asked if there would be any desire to change this decision. Chair Dew said there was not.

Mr. Schmid continued that the addendum to the investment policy statement had been approved at the April meeting and filed with the City. Once the small cap contracts are set, CapTrust will work with GTS to make a transition to the amended policy. There remains $7.5 million waiting to be called in real estate.

He recalled that Mr. Cypen had asked a question regarding the cash vehicle at the April meeting, and provided the Board with full information on the vehicle used by Northern Trust.

He moved on to alternative investments, noting that once this phase is underway, Artio and other managers will be brought in to present to the Board and a decision will be made on international managers. When new allocations have been finalized, CapTrust will work with Mr. Cypen and Ms. Bieler on a full revision of the investment policy statement. He characterized the recent addendum as a temporary measure until these changes can be made.

Alternative Investment Introduction

Chair Dew, Mr. Fortunato, Mr. Hole, and Mr. Burnam stated that as a matter of disclosure, they own Pimco mutual fund.

Mr. Schmid said CapTrust recommended diversifying what is already there, reducing the 10% weight to K2, and taking 5% out of the allocation to equities and moving this to alternative investments as well. This would bring total alternative investments up to 25%, which includes what is already in real estate as well as an additional marginal 10% that has not yet been discussed.

He stated when CapTrust runs its asset allocation modeling, the differences in risk return projections across various types of alternative investments are few. He stated when evaluating alternative investments, the main focus should be on making the Board comfortable with the vehicles that can offer the best possible liquidity terms, as well as the greatest transparency into what is going on, while keeping fees as low as possible.

Mr. Schmid pointed out that there was already hedge fund exposure through K2, and CapTrust was not looking at any additional hedge funds as part of this process. Instead they are focusing on tactical asset allocation and mutual funds, which provide a diversification benefit of daily liquidity and mandated transparency at approximately 85 basis points. Mr. Schmid asserted that CapTrust feels very strongly about this benefit. Other aspects of alternative investments that were initially discussed include income-oriented investments, such as preferred stocks and convertible bonds.

He continued that commodities generally have low correlation with stocks and bonds, and can do well in high-inflation environments. Mr. Schmid concluded, however, that CapTrust are very strong believers in private equity, which has historically outperformed the public markets; conversely, however, it also offers the least liquidity, and a commitment to a private equity investment is something of a perpetual process, as a five-year window would be necessary just to get the appropriate diversification.

Vice Chair Rudominer asked if there is a large enough mandate for private equity. Mr. Schmid said there was, and advised that CapTrust would achieve this mandate through the fund-to-fund route to get adequate diversification. He compared this to what has been done with the plan's hedge funds. He noted, however, that the private equity allocation must be built up over time, partly to stagger the liquidity and partly to get different vintage year exposure. While this asset class has good return potential, it can be time-consuming, and he reiterated that it is the least liquid investment.

He advised that among the managers to present to the Board in June, they would recommend Pimco, which also participated in the fixed income search some months ago. He recalled that while Pimco is a very good firm, the consensus had been that the intermediate duration bond portfolio was not the best use of them.

Vice Chair Rudominer commented that Pimco's holdings seem to correlate to what the plan already has. Mr. Schmid referred the Board to p.10 of the Alternative Investment Introduction, which shows all the funds in which Pimco is invested, and pointed out that they also offer exposure to some funds to which the plan has not previously been exposed. He concluded that Pimco would give exposure to a broader array of asset classes and attempts to add value by dynamically changing these allocations, including raising or lowering risk where it is appropriate.

Mr. Burnam asked how alternative bond strategies are defined by Pimco. Mr. Schmid said this group includes anything that is not in their standard, such as emerging markets funds, international bonds, unconstrained bond bundles, and others. He concluded that these are generally strategies that are beyond core plus investment grade bonds. Mr. Burnam noted that the average duration of unconstrained bonds is less than a year.

Mr. Schmid moved on to income-oriented investments, which include preferred stocks and bonds, multi-sector fixed income, and funds that are a mixture of assets. He advised that preferred stocks have done very well, particularly because all income-oriented investments have bond-like characteristics with equity-level returns. Preferred stocks have an adjustable rate component, and should perform well in a rising rate environment. He stated that the problem with pure convertible bond managers is credit quality, which can be lower than acceptable.

Mr. Burnam noted that an issue with preferred stocks is that most are either financial or utilities-based. Mr. Schmid agreed there is some sector concentration risk, and suggested that a 5% allocation would probably include preferred stocks in one of two ways: they can try to find a single manager who does everything well, or identify a manager who does well specifically in preferred stocks.

He continued that define Master Limited Partnerships (MLP)s have good income characteristics; however, one problem for institutional investors is that they had the potential of generating unrelated business taxable income (UBTI). Ms. Bieler explained that this would mean the Board was responsible for paying this tax, which would be generated by a business in which the plan becomes a shareholder. She emphasized that when managers present to the Board, they should disclose whether or not there have been any instances in which UBTI was generated. Mr. Schmid said he could ask managers of preferred stocks and MLPs to present to the Board in June as well.

He moved on to commodities, stating again that investing in commodities is less simple than it looks. Most of these investments are done through the futures market, which has a significant cost that eats away at the returns.

Chair Dew requested explanation of incentive fees. Mr. Schmid said hedge fund managers, for example, charge a management fee; there is also an incentive fee that is up to 20% of the profit. Chair Dew asked if there is any compelling reason to get involved with anything with this fee. Mr. Schmid reiterated that the fee comes from the profit: a manager takes 20% of profit while the fund retains 80%, and returns must be more than a certain percent before the incentive fee kicks in.

He continued that with commodities, there are passive or enhanced index funds, such as those held by Pimco; for other funds, commodities can add value through diversification, but the type of value they add is not the same as pure direct commodities. He suggested if Pimco discusses their all-asset fund, they should also be asked to spend some time discussing their commodity fund, although Mr. Schmid said he would not advocate bringing in a separate commodity manager for this purpose.

He said he would like to determine the Board's interest in private equity investment, particularly as private equity involves a longer process. He acknowledged that it might not be necessary for the plan, although it could improve

returns.

Vice Chair Rudominer asked if the fund is set up to take a hit to liquidity, which would come with private equity. Mr. Schmid pointed out that they were only discussing a 5% allocation. He added that private equity funds could also be invited to present to the Board and discuss various strategies.

Mr. Schmid said the target allocation for alternative investments is 25%, with 10% targeted toward real estate. The allocation to Long/Short has been reduced from 10% to 5%, which leaves 10% to allocate. He advised the Board to choose at least two different strategies, with 5% in a tactical allocation and the remaining 5% to another alternative of the Board's choosing.

Chair Dew asked what Mr. Schmid's recommendation for the remaining 5% would be. Mr. Schmid said they would first recommend the tactical allocation; after that, the choice would be determined by liquidity and the commitment to the process of building a private allocation.

Ms. Bieler advised that it is important for the Board to understand that private equity investments are longer-term and are not liquid; they cannot be liquidated as easily as other investments can be. She emphasized that there is not necessarily a ready market for private equity investments if the Board ultimately decides they do not like the investment and want out. There are often penalties involved, and sometimes a private equity holder can only get out when permission is given to do so. There is no direct contractual relationship with the entity that is making the investment, but instead shares are purchased from a fund, which is managed by entities owned by other entities. She explained that this is a deliberate creation of layers to insulate against potential liability. She concluded that it is best to have this knowledge before becoming involved with private equity.

Mr. Schmid agreed that with other funds, the plan can get its money out if they request it in advance, as with K2; however, private equity documents are written in a way that retains the option of not letting a plan take its money back.

Chair Dew likened this to getting into the queue for the real estate sector. Mr. Schmid pointed out that real estate investments, however, are semi-liquid and the plan could get its money back from that sector.

Chair Dew asked the Board members for input on the presentations they would like to hear in June. Tactical and private equity were requested.

Mr. Schmid reminded the Board that they will be getting 5% back from K2 at the end of July, which means they could put Pimco in place at that time and wait until a later time to allocate the alternative 5%.

The Board thanked Mr. Schmid and Mr. Woodruff for their presentation.

COMMUNICATION DIRECTOR'S REPORT:

None.

ADMINISTRATOR'S REPORT:

Summary Plan Description

Ms. Wenguer said she had received some feedback on the summary plan description that was sent to the Board members, including name changes. She advised that there would be a cutoff date of May 31 for further updates, as there will be additional changes to managers in the next few months.

Mr. Bayne suggested that Trustees' formal rank should not be listed, as they are not acting in a capacity other than that of Trustee. Chair Dew disagreed, pointing out that many individuals want to know what positions were formally held by the Trustees. Ms. Bieler said it was important to list the Trustees' names, Board positions (Chair and Vice Chair), and whether they are appointed by the City or elected; any other information should be what the members are comfortable with. It was agreed that further comments would be emailed to Ms. Wenguer.

Member Survey

Ms. Wenguer noted that recommended changes have been incorporated into the document.

Administrator's Contract

Chair Dew stated he had received one evaluation thus far. Ms. Wenguer said she would email evaluation forms to any members who did not have them.

PENDING ITEMS:

NEW BUSINESS

Mr. Hole requested an update on the payroll code issue discussed in April. Ms. Wenguer said they have identified the problem and are now aware of how to solve it; it is now waiting to be addressed by the Assistant City Attorney who handles pensions. Chair Dew said he had sent a request to the Assistant City Attorney approximately 10 days ago, asking that he review the situation and advise the Board of its status so they can move on appropriately. He has not yet received a response.

Ms. LeClaire said her office has been pursuing the issue of upgrade pay since August 2010, because while they are currently not taking out deductions on upgrade pay, employees are receiving the benefit of it in their pension calculation. She said a legal letter from the City Attorney's Office is required before they can begin deducting; the Assistant City Attorney may not have understood that the issue is also retroactive.

Chair Dew asked Ms. LeClaire to follow up with the Assistant City Attorney once again and copy him as well. He would then follow up with other City officials as needed. He thanked Ms. LeClaire for her assistance with the situation.

Mr. Hole asked for an update on the Memorandum of Understanding (MOU). Chair Dew said this is being rewritten as a proposal to the union contract rather than as an MOU.

Mr. Bayne asked if it has been confirmed that new employees are paying 8.5%. Ms. Wenguer said this has been checked as new employees were hired.

Old Business

Ms. Wenguer said the software RFP has gone out to bid and questions and responses have been received. She added that they are working to move much of the office into a virtual office, which will accompany the new software.

Mr. Bayne said Senate Bill 1128 has been passed to the Governor's office. He explained that there were "no touches" to the 175 or 185 money; there are some recording changes which would affect the Board. No changes are to be made in 2011.

Regarding communications to the City Commission, Vice Chair Rudominer requested that the following be noted: it has been verified by the actuary that the modifications made to the DROP plan have reduced the plan's unfunded actuarial liability.

Ms. LeClaire advised that in the past, the Board directs the actuary to calculate what the interest would be if the City paid it at the beginning of the year, quarterly, or otherwise; a decision is then made based upon the information presented to the City. She pointed out that it would be up to the Board to request that these calculations be made, as they would engender fees. Chair Dew observed that the benefit would likely outweigh the fee.

It was determined that Ms. Wenguer would find out the cost to perform this calculation before the Board directed Stanley, Holcombe & Associates to make this calculation.

Chair Dew requested concurrence from the Board that he make a short verbal presentation of the actuarial results to the City Commission.

There being no further business to come before the Board at this time, the meeting was adjourned at 3:37 p.m.

THIS IS IN RESPONSE TO CHAIRMAN DEW LETTER THAT WAS READ AT LAST MONTHS PUBLIC PENSION BOARDS MEETING.

I WAS surprised WITH THE LACK OF PROFESSIONAL COURTESY EXTENDED TO OUR BOARD OF DIRECTORS WHICH WAS TOTALLY UNCALLED FOR. IF THE COURTESY DISCUSSING THE TRUSTEES CONCERNS HAD BEEN PROFESSIONALLY EXTEND TO THIS EMBARRASSMENT AND AFFRONT TO OUR ASSOCIATIONS BOARD OF DIRECTORS AND ITS MEMBERSHIP COULD HAVE BEEN AVOIDED.

WE THE BOARD OF DIRECTORS PROUDLY LOOK AT OURSELVES FOR HAVING WITHOUT RESERVATION, REPRESENTED ALL RETIREES, IN ANY AND ALL MATTERS AFFECTING THEIR PENSIONS. THE BOARD OF DIRECTORS HAVE REPRESENTED, LOBBIED, A CAMPAIGNED, MET WITH CITY COMMISSIONER, ATTENDED MEETING, HELD MEETING, WORKED WITH ATTORNEYS, ATTENDED COURT HEARINGS, LET US NOT FORGET THIS ORGANZIATION FOUGHT THROUGH MULTIPLE POLITICAL AND LEGAL BARRIERS TO SUCCESFULLY WIN THE ME TOO AND THE ME TWO TWO, WHICH WAS DONE WHILE CONSTANTLY GOING UP AGAINST THE POLITICAL SPIN. BEING TOLD TIMING IS NOT RIGHT, ANOTHER ACTURIAL REPORT, PUT IT ON THE BACK BURNER.
THE HISTORY SPEAKS FOR ITSELF OUR MEMBERSHIP DOES NOT EVER HAVE TO WORRY THAT THIS ORGANZIATION WOULD FAIL TO REPRESENT THEIR INTEREST TO APPROPRIATE PARTIES.

IN RESPONSE TO THE FPPTA IT IS AN EDUCATIONAL GROUP WITH NON POLITICAL VIEW I AS TO THE AFFILIATE ASSOCATION OF RETIREES THIS ORG DOES NOT HAVE THE FUND TO ENROLL OVER 500 MEMBERS.

ALSO A FORMAL REQUEST TO THIS ADDED OR ATTACHED TO THE MINUTES.

Close Window