May, 2012

POLICE AND FIREFIGHTERS' PENSION BOARD
REGULAR BOARD MEETING
WEDNESDAY, MAY 23, 2012, 12:30 P.M.

Present
Michael Dew, Chair
Ken Rudominer, Vice Chair
Richard Fortunato, Secretary
J. Scott Bayne, Trustee
Jeff Cameron, Trustee
Dennis Hole, Trustee
Jim Naugle, Trustee
Steve Cypen, Cypen & Cypen, Board Attorney
Alison Bieler, Cypen & Cypen, Board Attorney
Lynn Wenguer, Administrator

Also Present
Amanda Cintron, Assistant Administrator
Laurie DeZayas, Pension Secretary
Doug Wood, Finance Director
Kevin Schmid, CapTrust
Stephen Schott, CapTrust
Randall Stanley, Nyhart
Michael Futterman, Marcum LLP
Alan Eichenbaum, Attorney
Amanda Lebofsky, Recording Secretary, Prototype, Inc.
John Stuber, President, Retirees' Association
Walt Courtney, Vice President, Retirees' Association
Fred Nesbitt, Director of Media Relations, Retirees' Association
Fuzzy Larkin, Retirees' Association
Jack Cann, Retirees' Association
Rick Schulze, Retirees' Association
Linda Soloman-Duffey, Retirees' Association
Gregg Gurdak, Retirees' Association
Bob Oelke

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 23, 2012, in the Pension Board Conference Room, 888 S. Andrews Avenue, Suite 202, Ft. Lauderdale, Florida 33316.

Communications to City Commission

The 2011 Audit was presented with a clean opinion. The actuary presented the five-year experience study. This study revealed that having members enter the DROP at a later time does indeed save the City money.

Pledge of Allegiance / Moment of Silence

Chair Dew called the meeting to order at 12:30 p.m. and roll was called. All present recited the Pledge of Allegiance and observed a moment of silence.

MINUTES: Regular Meeting: April 4, 2012

Motion made by Mr. Fortunato, seconded by Mr. Hole, for the waiving of the reading of the minutes as documented. In a voice vote, the motion passed unanimously.

BENEFITS:
Fire Department:

New Retiree (Term. of DROP):	Gregory C. Best
DROP Retiree:	William C. Humphrey
New Beneficiary:	Mary L. Houston
Retiree Death:	Glenn M. Gilley
Survivor Death:	Mildred Cowie

Police Department:

New Retiree (Term. of DROP):	Michelle Burgess
DROP Retiree:	Jack Lokeinsky
	Joyce L. Fleming
New Beneficiary:	Carol Knapp
Lump Sum Refund:	Dwight Isaac
	Luis Pagan
	Douglas G. Silk

Motion made by Vice Chair Rudominer, seconded by Mr. Fortunato, for approval of the benefits for Fire and Police. In a voice vote, the motion passed unanimously.

BILLS:

Lee Munder	$54,022.96
Agincourt	$46,784.02
Prudential	$40,471.92
Sawgrass	$35,562.00
Northern Trust	$31,126.79
Systematic	$26,438.64
Franklin Templeton	$22,979.28
InTech	$20,531.38
Eagle Asset Mgmt.	$20,299.26
CapTrust	$20,000.00
Boyd Watterson	$14,511.00
Atlanta Capital	$12,746.00
RhumbLine	$7,128.00
Marcum	$9,114.00
Marcum	$6,316.00
Ellen Schaffer	$1,265.00
Ellen Schaffer	$172.50

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

Ms. Wenguer noted that the accurate amount for the $6,316.00 bill by Marcum should be $6,325.00 as originally invoiced.

In a voice vote, the motion passed unanimously.

INPUT FROM ACTIVE & RETIRED POLICE OFFICERS & FIREFIGHTERS:

John Stuber, President of the Retirees’ Association, advised that input would be provided following the Cost of Living Adjustment (COLA) Report by Mr. Cypen.

2011 AUDIT REPORT: Marcum LLP Michael Futterman

Michael Futterman, representing Marcum LLP, stated that the Board members had copies of the combined financial statements for the Fort Lauderdale Police and Firefighters’ Retirement System and Supplemental Share Plan for the years ending December 31, 2010 and 2011. The document lists what was audited, as well as the standards under which the audit is performed.

The combined statement of Plan net assets shows what the Plan owns and owes as of December 31, 2011, along with changes in these assets. Mr. Futterman pointed out that the biggest change occurs in the net appreciation and depreciation of fair value investments, which decreased from $43.5 million in 2010 to $10.65 million in 2011. Net assets held in trust for pension benefits were roughly the same from 2010 to 2011.

Mr. Futterman continued that the remainder of the document describes the accounting policies followed by the Plan, as well as the governmental accounting standards under which the financial statements are prepared. An unqualified, or "clean," opinion is provided with regard to the financial statements. He briefly reviewed the management discussion analysis, which is a summary of activity for a given year and an explanation of why some items changed. A schedule of funding progress, which was prepared by the Plan's actuary, reflects the Plan's performance using the past six years of actuarial evaluations. He noted that the funded ratio of plans over the year improved from 2010 to 2011 by 2%.

Mr. Hole noted that the report specifically refers to future COLA benefits for individuals who retired after July 1986, and pointed out that a revision occurred in 2011, which should be specified in the statement. He observed that there was also a change in the contribution percentage for individuals hired after April 18, 2010. Mr. Futterman said the wording would be clarified as requested.

Motion made by Mr. Bayne, seconded by Mr. Fortunato, for acceptance of the audit with documented changes. In a voice vote, the motion passed unanimously.

Chair Dew noted that the Board has been served with an order to show cause, which is related to the case advanced by retiree Frank Colleran. Mr. Cypen and attorney Alan Eichenbaum, representing Mr. Colleran, briefly left the meeting to discuss this issue.

2007-2011 ACTUARIAL EXPERIENCE STUDY

Randall Stanley, representing Nyhart, stated that he would present both the five-year experience study and the draft Actuarial Report at today's meeting. Once the Board has approved the experience study, its results will be included in the Actuarial Report.

Mr. Stanley advised that the objective of the report is to ensure sound funding of the Plan. He observed that the experience study shows there were fewer retirements of both Police Officers and Firefighters than expected during the five-year span included in the report. This typically means individuals are retiring later than expected, which results in experience gains. He pointed out that in a poor economic climate, individuals often elect not to retire as quickly as they might otherwise.

Chair Dew asked if there was a source for the assumption that Police Officers and Firefighters were not retiring for economic reasons. Mr. Stanley said the tendency not to retire was reflected in the past five years, 2007-2011, but not in the previous five-year period. Chair Dew noted that the report states retirement significantly peaks at 20 years of service; however, he asserted that in Fort Lauderdale, 98% of individuals took additional DROP time rather than retiring, for reasons unrelated to the current economy. He felt the economic assumption was not applicable to the City, as the reason many individuals retired was because their terms of service and conditions dictated retirement.

Mr. Fortunato said he felt Police Officers and Firefighters were enticed to stay on the job longer due to staggering the DROP. Vice Chair Rudominer added that they must remain on the job past 20 years in order to maximize the DROP.

Mr. Bayne noted that in previous years, Police Officers and Firefighters were retiring at 20 to 21 years of service; however, attributing this strictly to the current economy was speculative unless the individuals were asked for their reasons. Mr. Stanley observed that the reason did not matter unless it resulted in the need to change an assumption.

He reiterated that the result of individuals' tendency not to retire resulted in experience gains; in the previous five years, there were experience losses. He said from an actuarial perspective, this meant no change in the assumptions would be recommended. Chair Dew stated that since pension reform has occurred, many individuals have

extended their service in order to maximize their benefits. Mr. Stanley asked if he felt this meant the next five-year experience study would continue to show this trend. Chair Dew confirmed this. Mr. Stanley said if the trend continued, it could be a reason for changing the assumption.

He continued that five years ago, assumptions were changed from being based on age to a basis of years of service. Actual turnover is currently less than expected, while the previous five-year study, it was greater than expected. In addition, the Plan has a net annual cost of nearly $1 million due to unfavorable turnover experience during the five-year period. While lower turnover is positive from a human resources perspective, it is a poor result with regard to funding a retirement system. The actuarial result is an experience loss. Mr. Stanley said this was also assumed to be attributable to the economy, which would mean no change should be made in the assumption.

Vice Chair Rudominer asked how turnover could be considered negative. Mr. Stanley said when individuals left their jobs and had no vested benefits remaining, they took their money with them. Chair Dew commented that he was also unsure this result could be accurately attributed to the economy.

Mr. Stanley moved on to mortality, noting that the current mortality table dates back to 1994. He pointed out, however, that mortality was not the most important assumption with regard to funding a plan. Typically, turnover assumption changes presume that individuals will live longer. Mr. Stanley stated that his recommendation for the Plan was to update these particular assumptions, but to refrain from expecting an improvement in longevity at the same time. He recommended that the table be updated to the RP-2000, noting that this would be accompanied by a new benefit calculation system, which would place benefit calculations on a consistent basis with funding assumptions.

He added that another recent adjustment pattern shows that blue-collar workers do not typically live as long as white-collar workers. There have been discussions suggesting that Police Officers and Firefighters should be considered blue-collar, which would lessen their life expectancy. Mr. Stanley noted that the larger an individual’s monthly benefit, the more his or her longevity was expected to improve. He concluded that he would not recommend considering Police Officers or Firefighters as blue-collar.

He advised that while the report assumes 100% of individuals in the Plan are married, this is not an accurate presumption. He estimated that 70%-80% are married; however, the 100% assumption is necessary due to other factors. No change to funding was recommended, although Mr. Stanley concluded that this factor could be better described.

He moved on to the economic assumptions, explaining that compensation increases may be due to inflation, merit, longevity, or other factors. Larger increases, such as those associated with merit, are typically seen in the earlier part of an individual’s experience. Increases due to inflation, however, would apply across the board over time. The average pay of continuing active Police Officers and Firefighters has increased by slightly more than 1%, although the table assumes 3.25% inflation. This means pay is not keeping up with inflation. Mr. Stanley concluded that this meant the inflation assumption is too high, and suggested that the percentage be reduced to 2.75%.

Mr. Bayne noted that the average inflation assumption, according to CPI, has been 2.5% for the last ten years. He asked why the assumption should not be lowered to this amount rather than 2.75%. Mr. Stanley said the inflation assumption is a component of the Plan’s investment return and interest discount assumption: if pay increase assumptions are reduced by 1% annually, the interest discount should be reduced by the same amount. He concluded that he would also suggest the pay increase assumption be reduced by 50 basis points, as the current rate cannot be expected to last unless it corresponds with inflation.

Mr. Stanley advised that the Plan has undergone a modest loss over the most recent five- and ten-year periods. The annual cost increase in 2009, in particular, was $14 million due to pay increases that were greater than assumptions. If not for these increases, the result would have been an annual experience gain due to compensation. It was noted that this result may be due to a 2009 employee count. Ms. Wenguer noted that it could also be due to a pay raise in 2008 that was not recognized until 2009. Mr. Stanley clarified that occurrences such as Me Too or Me Too 2 were not considered compensation experiences, but Plan amendment experiences.

He reiterated that the inflation assumption is considered too high, and should be decreased by 25 basis points, which would result in an immediate increase in the City's annual funding requirement. Mr. Stanley concluded that he would also recommend a 25 basis point reduction in the investment return assumption and a 50 basis point reduction in the salary increase assumption.

Chair Dew observed that the past 10 years have shown the worst market performance since the Great Depression, and asked if the changes to the assumptions meant this economic climate was expected to continue. He felt it could be a mistake to use the past 10 years as a point of reference for what will continue. Mr. Stanley said while he understood this point of view, the expected return, net of investment expenses, has been 7.8% for 10 years, while the actual return has been 3.8%. He felt the recommended decreases would be nominal.

He continued that the inflation assumption could be reduced while maintaining the same investment return assumption by increasing the risk premium or real return rate. This would result in no change to the interest discount assumption. He pointed out that it is the actuary's responsibility to ensure a reasonable discount rate that will lead to the maintenance of sound funding. He did not feel this approach was the same as looking to the past for justification of recommendations.

Mr. Stanley observed that all the actuarial recommendations led to an annual cost of approximately $1 million for the City. He noted that the City had made some prepayments that reduced their interest costs. Chair Dew asked if this meant Table 26 was not accurate at present. Mr. Stanley said the increments were accurate, but $1.8 million could be subtracted from each column. Chair Dew said because the document would eventually be published, he wanted to ensure the accuracy of these figures. Mr. Stanley said the figures in Table 26 would be changed for accuracy.

Mr. Hole commented that he had been on the Board 10 years ago when the rate was reduced to its current figure. He added that the Board operates under pressure from various sources, including actuarial standards. He referred to the table shown on p.9, and asked what the probability of achieving a 7.75% to 7.5% return would be if the figures were recalculated using the Plan's asset allocations. His concern was whether the Board is looking sufficiently far ahead or simply studying current economic conditions. He was also concerned that stagnation, as a result of high inflation and low growth, could occur in the current unpredictable market.

Mr. Hole continued that he was also concerned about increasing the City's costs when they are working to achieve more stability, as well as whether or not these costs were being allocated on an equitable basis. He did not believe lowering the return rate to 7.5% was too large a move to make at once, and noted that he might consider lowering it again in another five years. He felt this would ensure a reasonable margin if adverse expenses were incurred.

Chair Dew said he would like the Board to consider this option at greater length, as he did not feel there was a significant difference between 7.5% or 7.75% with regard to meeting the assumption rate. He concluded that he would like to consider the Board's options further, seek additional resources, and request input on this topic from the City Manager. He estimated that this conversation could be held at the Board's August meeting.

Mr. Cypen asked if it would concern Mr. Stanley to lower the salary assumption by 25 basis points while making no changes to the earnings assumption. Mr. Stanley pointed out that this would cost less. Chair Dew asked Mr. Cypen to investigate what the reduction in inflation, as recommended by Mr. Stanley, would do to the Plan. Mr. Stanley said this would leave the interest discount at 7.75% while reducing the salary scale by 25 basis points.

Mr. Wood advised if the Board approves a decrease in the rate of return, the 25 basis point difference would equal nearly $1 million. He said if this is not programmed when the budget process begins in July, it would likely not be available until July 2014, as the City's finances are short for 2012/13.

Chair Dew agreed that it would be very important for the Board to consider the City's contribution, as a change in the assumption could cost the City additional funds. He asked that Mr. Wood take the Board's discussion today back to the City Manager, and offered to meet with the City Manager himself. He stated that more realistic research and evaluation would be necessary before making a decision.

Chair Dew asked how long it might take Mr. Stanley to provide the Board with figures on the City's contribution if they approved a 25 basis point reduction in the salary inflation assumption. Mr. Wood advised that if the salary

assumption is reduced, the contribution on these salaries is also reduced, which increases cost.

Mr. Cypen clarified that the suggestion was to leave the discount earnings assumption the same while reducing the salary assumption by 25 basis points. Mr. Stanley said the result would be a reduction, which he did not recommend.

Vice Chair Rudominer asked from whom the Board would collect additional data and research with regard to Mr. Stanley's recommendations. Chair Dew said they would seek the City's input on this issue, as the proposed changes would not have a significant effect except with regard to the City's costs. He also felt this would be necessary because the previous ten years' experience was not considered indicative of future experience. He felt the previous 20-25 years would need to be investigated in order to accurately show the Plan's value.

Mr. Naugle commented that the recommended decreases in assumptions appeared to be good advice, and the sooner these changes were known, the easier it would be to plan and budget for them. Chair Dew concluded that he would like to hear the City Manager's input on the recommendations before making a decision.

Mr. Stanley suggested that the Board also discuss the recommendations with their investment consultants. Mr. Schott pointed out that bond yields are currently at historic lows, while equity valuations appear to be more attractive; over a five-year term, however, if rates increase and equity valuations remain positive, he felt the asset allocation CapTrust had presented to the Board "would still be obtainable."

Mr. Schmid added that there are three components related to meeting the 7.75% actuarial return: what the markets give, the performance of active managers over what the markets give, and the benefits gained by a disciplined rebalancing of the portfolio. He pointed out that a 25 basis point change to the actuarial assumptions would apply a great deal of precision to a relatively imprecise science: its single definite effect would be to raise the City's contribution.

It was noted that the City Commission would begin discussing the budget at their first meeting in July. Mr. Wood offered to take the information presented to the City Manager, with comments, so he could explain the rationale behind reducing the return rate from 7.75% to 7.5%. This change would have the greatest single impact on the City's budget, although Mr. Wood noted that changing the mortality table would also increase costs. He advised that the budget would be in draft form until August, which meant it could be changed if outstanding issues were identified.

Mr. Hole asked what the probability would be of the Plan's reaching 7.5%. Mr. Schmid said CapTrust could run simulations to determine this. He felt it was necessary to reach an equitable balance rather than failing to address this issue. Chair Dew emphasized while he did not want to unnecessarily delay a decision, he felt input from the City was crucial.

Vice Chair Rudominer observed that if the actuarial recommendations were adopted, the percentage of payroll would initially increase. Mr. Stanley confirmed this, noting that adopting the recommendations would result in reduced probability of experience losses in the future. In ten years, the Plan would still use 7.5%, which is a more conservative basis. The Plan would also have more assets, as the incremental amount would have been funded for ten years. He estimated that the more conservative basis would probably be marginally lower, depending upon the Plan's investment return.

Chair Dew asked if the Board could make another change in one or more years if they felt the basis required reevaluation. Mr. Stanley said this would be up to the Board. Chair Dew reiterated that while the Board is in agreement on updating the mortality table, he felt it would be best to discuss the other recommendations with the City Manager and bring these discussions back to the Board before a decision is made.

Mr. Wood asked to see the numbers associated with both a 7.5% and 7.75% basis for side-by-side comparison. Mr. Stanley noted that this is included in the report. Chair Dew confirmed that a change would increase the percentage of payroll; The change in the mortality assumption would equal roughly a $55,000 increase.

Chair Dew concluded that following his discussion with the City Manager, he will report back to the Board.

Vice Chair Rudominer asked if the asset allocation would need to be changed accordingly. Mr. Schmid said a 25 basis point change in the actuarial assumptions would not require a change in the asset allocation, as it would not affect return on the Plan. Mr. Stanley added that investment policy should not be set according to actuarial assumptions; instead, he recommended that assumptions be set according to investment policy.

Motion made by Mr. Fortunato, seconded by Mr. Bayne, for the correction and the changes that the Board discussed, including Table 26, and also the acceptance of the new mortality assumptions to the 2000 level.

Mr. Stanley pointed out that the annual actuarial report, dated January 1, 2012, has not yet been finalized, pending the Board's decision on assumptions.

In a voice vote, the motion passed unanimously.

Mr. Bayne asked if the revised report could be provided by the next Board meeting. Mr. Stanley said it could.

2012 ACTUARIAL REPORT: Randall Stanley

Mr. Stanley advised that in 2011, the report began to disclose the cost of DROP as a percentage of total payroll. The payroll of DROP participants is just below $8 million. There is also a projected payroll, as the State requires actuaries to monitor and calculate minimum funding based on this percentage of total payroll.

He continued that the most important news included in the report is the actuarial asset value of $505 million, with a market value of $453 million. The $505 million figure represents the smoothed method, and is roughly 112% of the market value. This is an increase from the 106% figure one year earlier.

Mr. Stanley explained that the smoothing method dampens the volatility of City contribution requirements in a very effective manner. This prevents the Plan from increasing or decreasing at the same rate as the market. The asset value was at 112% of market value as of January 21; the State will not allow this value to surpass 120%. If this limit is reached, volatility is no longer dampened.

He advised that the present value of total projected benefits is $858 million for all members included in the system. This is the funding target, although it is not a target that can be reached. Accrued liability makes up a part of each member's liability, as that individual has future service that will accrue.

When the smoothed asset value of $505 million is subtracted from the $700 million in accrued liability, the result is an unfunded liability of roughly $200 million. If the changes recommended in the experience study are made, this figure will increase, as the recommendations are more conservative than the present assumptions.

Mr. Stanley moved on to the detailed gain/loss analysis, noting that the most important aspect in this area was investment return. A contribution of $31 million was expected from the City, but a $31.1 million contribution was actually made, as the experience loss increased the annual contribution. Another noteworthy item was interest savings to the City due to prepayment of the contribution.

Chair Dew said the Board would get in touch with Mr. Stanley if additional questions arose in relation to the 2012 Actuarial Report or the Experience Study.

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

Order to Show Cause – Frank Colleran

Mr. Cypen addressed the order to show cause with regard to Mr. Colleran's case. He stated that he and Mr. Eichenbaum had discussed the potential resolution and settlement of the case; Mr. Cypen had advised Mr. Eichenbaum to contact Mr. Colleran with regard to this issue. He expected there would be additional information to report to the Board no later than the next scheduled meeting.

Vice Chair Rudominer requested clarification of the order to show cause. Mr. Cypen explained that this court order requires the Board to show cause why Mr. Colleran should not receive the relief he is seeking. The result is an

extension, based upon Mr. Cypen's discussion with Mr. Eichenbaum.

Chair Dew stated if there was a cost associated with the order, he would like the Retirees to understand it might have negative ramifications with regard to COLA, as this cost is included in the overall investment cost. Mr. Cypen advised that no details of the case should be discussed with the public.

COLA REPORT: Steve Cypen, Alison Bieler

Ms. Bieler noted that the Board members had been provided with copies of a memorandum reviewing past cost of living adjustments (COLA). She emphasized that the memo does not determine whether or not the COLA calculation was made correctly during any given year: its intent was to review COLA from the time it was first adopted until the present. She noted that a second attachment lists all documents provided by the Pension Office and used in preparation of the memo.

Ms. Bieler gave a brief overview of COLA, stating that it was originally adopted in 1972. The Plan did not have a COLA provision prior to this time. A new COLA was adopted in 1986 with different features, including a sunset clause. The clause provided that the new COLA would sunset on July 1, 1991, unless it was re-adopted by the City Commission.

The 1986 COLA was amended in 1987 in order to allow the Board to make payments using different distribution methods. Before this time, the COLA benefit was only added to the monthly retirement benefit; however, the new provision allowed the COLA to be paid by lump sum, no more than twice. After the two lump sum payments, the Board would then have the option of paying the COLA by adjusting the monthly benefit so every retiree was paid the same amount, or on a graduated scale based upon how long an individual had been retired.

In 1992, the pension plan and COLA provision were again amended with the intent of providing different distribution options. Only two limitations were given to the Board with regard to these payments: the total sum paid out by the Board could not exceed the actuarial equivalent amount generated by the applicable COLA computation formula, and the Board could choose whether they would give all retirees the same equal amount or a graduated benefit. In 1992, the sunset was extended to 1994; in 1994, it was extended to 1997.

In 1996, the last COLA amendment changing the actuarial formula occurred when the City Commission changed the actual formula used to calculate the COLA. Ms. Bieler read the City Commission's statement on this amendment, which allowed the Board to look at only one prior year in the event that three or more years were subjected to asset smoothing. She noted that the City Commission recognized this amendment would be applied to the 1995 COLA.

Also in 1996, the City Commission extended the COLA to 2000; in 2000 it was extended to 2005; and the last COLA adjustment received by any retirees was paid in 2001 for calendar year 2000. The City Commission continued to extend the COLA's sunset provision even though no COLA adjustments were made, so the calculations would continue to be done. The most recent extension was made on July 17, 2007 and extended the sunset provision to July 15, 2008. In 2008, the City Commission amended COLA a final time, adding a provision that stated no COLA may be granted, authorized, paid, or distributed during the calendar year 2008. The COLA was then allowed to sunset, which meant it was automatically repealed.

Ms. Bieler reviewed the Florida law applicable to the Plan, noting that it is a defined benefit plan under 175 and 185 of the Florida statutes, and is governed by Chapter 112, Part 7 of these same statutes, the Florida Protection of Public Employee Retirement Benefits Act. She explained that this Act was adopted in 1978 for the purpose of implementing a Constitutional provision dealing with pension plans. This provision is included in the COLA memorandum.

She explained that the Act preempted any conflicting local laws that may have been in existence at the time. She explained that this is known as express preemption, which clearly shows all public pension plans must comply with its provisions.

The most recent amendment to the legislative intent section of this Act came in 1994, and refers to the use of actuarial experience to fund additional benefits. This amendment, like the preemption provision, has not been

changed since its adoption.

Taking all the changes to COLA over time into account, including Florida statutes and case law, Ms. Bieler stated the legal conclusions. COLA is a contingent benefit by design: it is not a guaranteed or fixed percentage, as it is contingent upon how the funding mechanism pans out during any given year. Also, it was originally adopted with a sunset provision that provided for an automatic repeal, which meant it was never guaranteed beyond a particular date, even if the funding requirement was met.

Upon reviewing the pension Ordinances, Ms. Bieler stated that it is clear the Board was given the authority by the City Commission to determine only the distribution methods for COLA, whether as a lump sum, an addition to the monthly benefit, a graduated benefit, or by another method. At no time, however, was the Board granted authority over the funding formula set forth in the Ordinance.

The 1994 amendment to the Florida Protection of Public Employee Retirement Benefits Act now governs how the COLA benefit is calculated. Prior to this Act, the provision that required an accumulation of actuarial experience from all sources did not exist. Once the amendment to the Act was adopted, actuaries were required to make this calculation with a view toward what was allowed by Florida law, rather than what was previously allowed by the Plan. The calculation made in accordance with the State statute controls whether or not COLA may be paid, as all accumulated gains and losses from all sources must be taken into account by the actuary. She concluded that all actuaries appear to have calculated the COLA in a manner consistent with this law.

Mr. Hole noted that the document referred to a case currently before the Florida Supreme Court. Ms. Bieler explained that this case challenges the Florida Retirement System's ability to make certain changes, one of which is related to payment of COLA. A ruling is expected to be issued before the end of the calendar year. She noted that there is a possibility, depending upon the scope and extend of the Court's decision, that the case could affect the information included in the memo.

Chair Dew asked what the Board would need in order to be able to pay COLA. He noted that the memo states it is subject to the total gains of the Plan, after all expenses have cleared, and then goes through an actuary analysis. Mr. Stanley referred the Board back to the draft Actuarial Experience Study, noting that these calculations were shown beginning on p.41. There is a deficit; the number must be positive to result in a COLA from gain sharing. He observed that the number becomes lower each year the calculation was made.

Mr. Wood left the meeting at 2:47 p.m.

Mr. Stanley continued that in order to pay a COLA, the current $146 million deficit in gain sharing must first be eliminated through favorable experience. He advised that the only other way of which he was aware was an ad hoc COLA, which would require approval by the City. He suggested that an amendment could be formulated to create an automatic COLA, but this would require City approval as well. Ms. Bieler noted that the Plan's COLA, from the time of its inception, was never a fixed amount, but was a function of experience.

Alan Eichenbaum, attorney for the Retirees' Association, explained that many retirees felt when they were eligible to retire, the formula that applied to them at that time should continue to apply, even if it has since been amended.

Chair Dew noted that the memo states Florida law supersedes this. Mr. Eichenbaum pointed out that the Florida law did not take effect until 1994, and there are retirees who were already eligible prior to that time. He felt the State law was not applicable for this reason, as it could not override these benefits.

Ms. Bieler stated if a COLA benefit was in place at the time of an individual's retirement, they would still be eligible to receive COLA if the calculation warranted it. She noted that the actual formula did not change until 1996, after Chapter 112 was amended; the only change prior to 1996 was related to the distribution methods the Board could use to pay the COLA. There have been no further changes to the formula.

Mr. Hole asked if an individual who had retired in 1971 would be eligible for the COLA benefit enacted in 1972. Mr. Cypen said this benefit would be covered by the Me Too provision. Ms. Wenguer clarified that Me Too was always included in the contract until its removal in 1994.

Mr. Eichenbaum asked if those individuals who retired prior to 1994 would be subject to the formula that applied when they retired, or if the formula from 1996 and afterward would be used. He explained that some individuals who retired prior to 1994 felt the actuary was not comparing the two formulas to determine which one is more beneficial for them.

Mr. Stanley pointed out that no COLA has been granted since he has acted as the Board's actuary, which meant he had not dealt with either formula. He noted that the formula to determine a cumulative loss or gain of experience is actuarial math. Mr. Eichenbaum asked if a different form of actuarial math would be applied to individuals who retired before 1994. Mr. Stanley said unless there was a cumulative experience gain, the question appeared to be moot.

Chair Dew asked if there was, hypothetically, a COLA, whether or not Mr. Stanley would apply the same math to pre-1994 retirees as he would to post-1994 retirees. Mr. Stanley said he had not considered this question, as there had not been a cumulative experience gain. Mr. Naugle commented that should the Plan achieve 100% funding, they would then need to determine the appropriate formula or formulas.

Vice Chair Rudominer noted that before COLA could be applied, the Plan would have to make up its $114 million unfunded liability. Chair Dew said this was not necessarily the case. Ms. Bieler said the part of the formula that existed prior to 1996, which includes a provision for gain sharing was still subject to Chapter 112. She added that COLA was never guaranteed and is always contingent.

Mr. Hole asked if the COLA issue had gone to the unions for approval, as it consisted of an Ordinance change affecting benefits. Mr. Cypen said while language in the union contract might address the issue, it did not have the authority of law unless it was part of the Ordinance.

Ms. Bieler said when the final change was made in 1996, there was extensive discussion at Pension Board meetings, including conversations with the City Manager. It was eventually determined that if the change had not been made, no COLA would have been paid for 1995. She stated that the discussion clearly shows the change was made so a COLA could be paid to retirees for 1995.

She reiterated that the original COLA was amended in 1986 to include a new formula, which is still in existence with one additional change. She referred the Board to p.2 of the COLA Report, which shows the formula. It also defines the term "excess gains" as a three-year average. The 1994 amendment to Act provides that excess gains must be determined in accordance with the State law and all local Ordinances were preempted.

Mr. Bayne asked if anyone retiring prior to 1994 would be affected by the change in the future. Ms. Bieler observed that COLA was never taken away as a benefit, and is calculated each year to determine whether or not a benefit can be paid. The legislative change states that after 1994, COLA must be calculated subject to new requirement of the Act.

Mr. Bayne requested confirmation that retirees prior to 1994 were still affected by the change. Ms. Bieler said it would be incorrect to state whether or not these individuals were affected: if they were entitled to a benefit, they have already received it as the COLA is paid year by year. Mr. Bayne asked if a 1993 retiree would still be affected by the law applied in 1994. Ms. Bieler confirmed this, reiterating that calculations were already done and benefit had already been paid to retirees prior to the change in state law.

Chair Dew clarified that the question at hand is how many COLA formulas could presently be used if benefits were to be calculated. Mr. Eichenbaum added that his question was whether the language change in 1994 affected the calculation for individuals who had retired before that time. He explained that he wanted to know if the change would be more beneficial to pre-1994 retirees than the language in use at the time they retired.

Ms. Bieler said based upon the documentation she had reviewed, there would have been no COLA paid in 1995 if the change had not been made. She stated that she could not answer this on an ongoing basis, as she was not an actuary.

Mr. Eichenbaum asked if it would be possible for Mr. Stanley to explain the differences in the pre- and post-1994 formulas to the retirees, and how these differences would affect the determination of COLA. He advised that many

retirees feel they were being denied a COLA benefit to which they were entitled.

Mr. Stanley clarified that the word "provided" in the change referred to a cumulative experience gain. Should this term be removed from consideration, he pointed out that there were years in which there was an experience gain; had the proviso not required the experience gain to be cumulative, he felt there may have been additional years in which COLA could have been granted.

Ms. Bieler said regardless of whether the language was changed in 1996, the calculation would still be subject to whether or not there were accumulated experience losses, which would mean COLA could not be paid. Mr. Eichenbaum argued that this State law would not have an impact on individuals who retired before the language took effect. Ms. Bieler said it would, because when COLA was reenacted in 1996, it became subject to the State statute.

Mr. Cypen commented that perhaps the upcoming State Supreme Court decision would include language that would be beneficial to resolving this issue. Mr. Eichenbaum pointed out that Mr. Stanley's statement implied those retirees for whom the proviso was not in effect might have received COLA were it not for the additional language. Mr. Cypen said because COLA is conditional, it was his opinion that individuals who retired before 1994 were affected by the change, as were retirees after that time.

Mr. Fortunato asked why individuals who retired prior to 2008 remain eligible for COLA if it is a conditional benefit. Ms. Bieler said because these retirees were eligible to retire before COLA was allowed to sunset, they retained the right to the COLA calculation; however, due to funding, they have not been able to receive a COLA.

Mr. Eichenbaum confirmed that his question regarding COLA had been answered by Mr. Stanley, Ms. Bieler, and Mr. Cypen.

At this time the Board took a brief recess from 3:30 p.m. until 3:41 p.m.

QUARTERLY INVESTMENT REVIEW CAPTRUST: Steve Schott, Kevin Schmid

Mr. Schott reported that yields are presently at historic lows, noting that three-month Treasury bills, for example, are currently paying 0.02%. In 2011, Treasury yields were at 3% before their downgrade. He stated that this does not mean they will not increase significantly, and noted that a reasonable increase in Treasury yields is historically favorable for pension plans, many of which are valued against corresponding government and corporate bonds.

The market overall had a particularly good quarter, with the S&P up to 12.6%. Since March 2009, it has nearly doubled; however, the annualized figure from five years ago was 2%, and only one to two years past, the market showed negative or even returns.

Large- and mid cap performed well over the past year, as did international markets, although domestic markets continue to outperform international markets and are up 8.5%. Mr. Schott pointed out that due to valuations, international markets may be more attractive than domestic, although they have been penalized for being based overseas. He stated that valuations have always trumped bad economic perspectives over time.

While benchmarks appear positive for the quarter and the year, on a five- or ten-year basis they remain in the 3%-4% range. Even funds with significant allocations in alternative investments have been affected. He suggested that the allocation changes the Board has made over the past year have had an overall positive effect on the plan.

Mr. Schmid agreed, recalling that at the recent investment workshop they had referred to 2011 as a transitional year. The Plan is now fairly close to its goal for allocations. For the quarter, the Plan was up 7.2% net of fees against a 7.6% policy index. Manager performance was relatively strong, save the alternative assets such as the Pimco All Asset Fund and K2, which did not keep up with some markets. Mr. Schmid said while their performance was not where they had hoped it would be, their returns were not highly negative.

The Plan remains slightly overweight in large cap equity and underweight in international and real estate; cash is at roughly $8 million. CapTrust did not have any asset allocation recommendations to make at this time.

InTech was up11% in large cap, mostly due to sector allocations, as they were underweight in technologies and overweight in defensive strategies; however, over the long term they have exceeded their benchmark. Sawgrass was 2% behind for the quarter against their benchmark of 14.7%. Mr. Schmid noted that this was not a market in which Sawgrass could be expected to outperform, and for the year they are 4% ahead of their benchmark. Stock selection in technology held them back during the past quarter. He noted that their benchmark is becoming highly concentrated in technology as a sector, but they are only allowed to hold 5% allocation in this sector at this time due to CapTrust's IPS limits.

He continued that Sawgrass has informally requested permission to exceed this 5% technology allocation; without it, they must sell any overage immediately. As a stock reaches its allocation limit, it must be trimmed back in order to remain within portfolio guidelines. Mr. Schmid said this problem is faced by all large cap growth managers at present. Sawgrass has not taken any action that would exceed their limit or place them out of balance, and remains within policy. Mr. Schott concluded that CapTrust is not recommending any changes, but wished to make the Board aware of the situation.

Chair Dew stated that he was very disappointed in manager performance, as no managers reached their benchmarks and the Plan remained 4.5% below the S&P despite the strong quarter. While there have been sector transitions and changes made, he asserted that he was becoming frustrated, as the Plan is currently unable to reach the 50th percentile. He expressed disappointment that this lag occurred within a strong quarter. He asked that the CapTrust explain why some managers were not on a watch list, and whether or not enough is being done to allow the Plan to make money. Chair Dew concluded that some corrective action must be taken.

Mr. Schmid said only 45% of the Plan's assets are in the equity market, which means only that percentage is invested in an up market. The 30% invested in fixed income, for example, only earned 1% the past quarter. Because this fixed income acts to stabilize volatility, he did not feel the Plan could support the risk of being more heavily invested in equities. He estimated the Plan had lost 3% to 3.5% thus far for the present quarter.

Chair Dew said the Board and CapTrust should review whether the Plan is invested in the right managers, and stated again that perhaps they should address what is going on with the Plan's performance so it can earn money. While he did not wish to add too much risk, he felt the present performance required further review.

Mr. Cypen observed that the disclaimer information in the report's table of contents states the report is provided as a courtesy, and noted that an appendix refers to violations of guidelines. Mr. Schmid said he would address this issue with CapTrust's compliance department, and stated that the appendix should note that there were no violations to report at this time.

Mr. Schmid returned to the large cap managers, which lagged 1.5% to 2% behind their benchmarks. InTech is still ahead of their benchmark on the long-term average. Sawgrass, which has been in the Plan for five years, has lagged, although last year he recalled they were the best-performing manager in the Plan. He recalled that Sawgrass's reasons for underperformance have been discussed at prior meetings; CapTrust remains comfortable with them and does not have them on a watch list due to their recent performance. He felt their investment style is beginning to be rewarded.

Chair Dew stated that since inception, Sawgrass has underperformed. He referred to p.44 of the report, noting that their performance has not approached the 50th percentile. He felt CapTrust was too comfortable with Sawgrass's tendency to lose money. Mr. Schmid said they were comfortable with Sawgrass despite the performance lag because they have also taken much less risk than other managers. He noted that in general, their investment style is more protective on the downside and does not perform well in an environment where lower-quality stocks rally, such as in 2009, 2010, and the past quarter. He asserted that their relatively lower risk can be beneficial to the Plan.

Chair Dew noted Sawgrass's ranking in comparison to other managers. He stated again that they continue to lose money, despite their investment fees. Mr. Schott said when CapTrust inherited the Plan's portfolio, Sawgrass was a poorly-performing manager, and they have often continued to be so over the long term; however, CapTrust felt if the Plan holds onto them as a manager, they will cycle back to stronger performance. He recalled they were in the top 20% of managers in 2011. He did not want to fire a manager before they have the opportunity to turn their performance around, although this may be frustrating over the long term.

Chair Dew suggested that Sawgrass go on a watch list, as he felt the Board is failing in fiduciary responsibility if they do not address this lack of performance. Mr. Schott reiterated that managers such as Sawgrass balance the risk taken by the Plan in other allocations such as equities.

Mr. Schmid moved on to Systematic, which performed poorly in 2011 but has surpassed their benchmark by 4% thus far in 2012. Their longer-term performance has added nearly 2% per year for the 10 years then have been in the Plan.

Chair Dew asked to know the difference between InTech and Rhumbline. Mr. Schmid said Rhumbline is a pure index fund, while InTech is actively managed on a quantitative basis. InTech might be redundant in the plan as equities were reduced; however, over the long term they have added value to the Plan. He advised that the equity portfolio should have a mix of index and active strategies. InTech and Rhumbline also help in dampening the relative volatility of the entire Plan. He noted that since inception, they have added value over their benchmarks and do not charge significantly from a cost standpoint, although he felt this potential redundancy could be reviewed at a later time.

Mr. Schmid noted that several recent changes have been made to small- and mid cap over the last five quarters, including the removal of NorthPointe. He advised that there has been more change than they would have liked, such as the termination of Franklin Templeton due to their portfolio management change, despite Franklin's strong performance during a short time period. Funds from Franklin Templeton were moved to Eagle Asset Management, which has outperformed their benchmark in the last quarter. Lee Munder has also outperformed their benchmark by over 2%, one of the best performances in the plan.

He recalled that Artio was terminated at the end of 2011 and replaced with Lazard International, which has added value in the four months they have been in the portfolio. Thornburg is ahead of their benchmark for the quarter but behind for the year. He reiterated that on the fixed income side, little return was generated in the last quarter, and may become even lower in the present quarter due to pessimism over issues in Europe and the tendency of the Federal Reserve not to raise rates. Agincourt, Boyd Watterson, and Atlanta Capital were added as defensive managers, although Atlanta Capital has been terminated and its portfolio was consolidated with Boyd Watterson. These defensive managers have also acted as a drag on the portfolio's performance, although they have lessened the impact of volatility in other sectors.

In real estate, Mr. Schmid noted that fixed income is viewed as safe in comparison to other risk asset investments; real estate has contributed a solid return over the last two years without experiencing the volatility of the equity market. Income-producing properties are up roughly 2% against their benchmark. Most of their return is income-based, with some capital appreciation built in as recovery in the real estate market continues. He cautioned that double-digit returns are not to be expected in this market. In their five years in the Plan, real estate has been a negative contributor overall. In 2009 in particular, he recalled that the real estate portfolio was down over 40%.

Mr. Schmid said he was comfortable with the Plan's target real estate allocation of 10%, as it takes some risk and can produce returns; it is, however, often a different type of risk from the equity market. In normal environments, such as the third quarter of 2011 and the current quarter, when equity markets are down, real estate should return 2% to 4%. This is why it is part of the Plan: its asset class is a diversification from a risk standpoint.

Mr. Fortunato asked if real estate was overallocated at present if its performance is low. Mr. Schmid said he would not recommend taking money from fixed income and putting it in a more volatile allocation such as real estate. He pointed out that in a 2008 scenario, only fixed income had protected the plan, although its yield is dramatically low. He reiterated that its place in the plan is to act as a volatility shock absorber.

Mr. Schmid said it was a good quarter for the Pimco All Asset Fund, which was up 6.5%. He noted that this fund is another form of diversification, as they are invested across several different asset classes to which the Plan would not be otherwise exposed, including emerging markets and commodities, although they cannot keep pace with the equity market at present.

With regard to K2, he recalled that there had been discussions about bringing firms in to discuss shifting from long/short to a diversified hedge fund strategy, and there is continued interest in having different types of managers make a product presentation to the Board. This could help them decide if it is necessary to move on to more

diversified strategies, as it has been difficult to make money in long/short in recent years. He suggested that CapTrust could identify two to three hedge fund managers to invite to the June meeting, or at a later time if the Board wished.

Ms. Wenguer advised that the Agenda in June is relatively open. Chair Dew asked that EnTrust be invited to make another presentation to the Board. He recalled that their previous presentation had been for informational purposes, although their second presentation could be made as a pitch.

Mr. Fortunato asked if there was a lockup of funds with K2 that should be redeemed right away. Mr. Schmid said this redemption would make sense if the Trustees are committed to moving away from this manager.

Mr. Hole noted that Pension & Investments reported two other Boards have pulled $1.2 billion from K2 recently. Mr. Hole also reported receiving information from GTS that the plan had saved $40,000. Chair Dew asked that any Trustee receiving information from a manager have them send that information to Ms. Wenguer as well so it may be shared with the Board.

Mr. Schmid said if the Board terminated K2, the Plan would likely have another manager in place by the time the 90 day time frame was up to get their money back from K2. If no manager was selected or contracts were not in place, the money could be moved to the Pimco All Asset Fund for the time being.

Motion made by Mr. Fortunato, seconded by Mr. Hole, to terminate K2 with the proper notice. In a voice vote, the motion passed unanimously.

Mr. Schmid said he recommended termination of the long/short asset class. He advised that K2 has asked to be considered in the hedge fund space. Chair Dew said once a manager is terminated, the Board would not like to consider them further.

Chair Dew asked if the S&P is an appropriate benchmark. Mr. Schimd said it can be over the long term, such as a full three- to five-year market cycle. On a quarter-to-quarter basis, however, it is an unfair benchmark.

It was determined that three money managers, including EnTrust, would be invited to present at the June meeting. Long/short will be dropped altogether, although it will likely remain a component of a multi-strategy hedge fund approach. Mr. Schott said the purpose of a hedge fund strategy is to diversify the plan’s overall risk by taking money exposed to the equity market and diversifying it. Long/short has only stock selection at their disposal, which is difficult in the recent economic environment. A multi-strategy approach diversifies the overall risk profile of the plan, and expands the opportunity set by making money on mergers and acquisitions, bankruptcies, and other actions.

Chair Dew asserted again that he was frustrated because recent changes, approved by CapTrust, did not help the Plan, and asked when the Plan might see more of a benefit. Mr. Schott said it can be slow to make progress in the current environment, although he felt the Plan would see marked progress over the longer term.

Mr. Fortunato asked if there were other actions the Plan should take than what was being done now. Mr. Schott said most firms using similar capital market assumptions were not acting as outliers at present without having taken extraordinary risks.

Mr. Hole said he had spoken with investors in agricultural and infrastructure assets, and asked that CapTrust consider these asset classes. Mr. Schott said they would review two particular funds, Omar and Hancock Agricultural Investment Group, noting that some people think agriculture has potential to be a strong market. He felt from a macro perspective with stocks and bonds, the Plan might consider adding these; now that the overall allocation is in place, they could also consider energy and private equity.

Mr. Schmid said agricultural and infrastructure funds might be included in the real estate allocation, and noted that the returns on agriculture have not been what might be expected. He added that United States infrastructure grades are low, but there has been no sweeping reinvestment in this segment to address it due to the current fiscal climate. He noted that global infrastructure might be more profitable than domestic.

COMMUNICATION DIRECTOR'S REPORT

Mr. Nesbitt said he was recently complimented on the Plan's website, particularly with regard to its transparency and the information provided. There was interest in a potential news story on pension websites, using the Fort Lauderdale site as an example. Chair Dew asked to be kept apprised of this possibility.

ADMINISTRATOR'S REPORT:

Contribution Arrears Payment

Ms. Wenguer said the contribution arrears repayment had to do with members that have terminated their employment. If they are on leave, or suspended, they must continue to contribute to the pension to get their service credit, as stated in the Ordinance. She asked how long these individuals may be given to pay arrears, noted that they are vesting and not collecting during this time.

Mr. Cypen said this was typically determined by a formula based on the length of time in question. If they are suspended without pay, the plan says they will receive credit for periods of suspension. This could also be offset against that person's retirement benefit. Mr. Cypen said they should pay before receiving benefit. The Board members discussed whether or not this would apply to an individual whose employment is terminated at the end of his or her suspension.

Ms. Bieler said a member must continue to contribute his earnings to the plan in a manner approved by the Board, with the exception of time served in military service. Chair Dew noted that this might refer to suspension with pay. Ms. Wenguer said this was not specified. It was stated if individuals are suspended without pay, they must continue to pay out of pocket, similar to health insurance.

Ms. Wenguer said in the past, when a person is readmitted following suspension, their first check is often wiped out by the payment in arrears. If it did not, they were asked to double their contributions until arrears have been paid in full, and they are given the same amount of time that they were out to complete these payments.

Ms Bieler offered to draft an arrears policy for the Board. Chair Dew asked that Ms. Wenguer work with Mr. Cypen and Ms. Bieler to review and arrive at appropriate language for this Item, which would be placed on the following month's Agenda for further discussion and clarification.

City Network Connection

Ms. Wenguer recalled at the last meeting, the Board had approved an expense of $3200 toward the networking upgrade. The City is doing a system upgrade, of which the plan must pay its share. The cost is a one-time charge of $5200, which will include upgrades to both the phones and internet.

Motion made by Vice Chair Rudominer, 2nd by Mr. Fortunato, to accept the upgrade for the $5200. In a voice vote, the motion passed unanimously.

New Business

Mr. Hole said he, Vice-Chair Rudominer, Chairman Dew, and Ms. Wenguer had attended the NCPER's annual conference, and that he and Secretary Fortunato had attended the Division of Retirement annual conference. Mr. Hole reported that both seminars were informative, educational, and had provided valuable networking.

Mr. Hole also gave Ms. Wenguer info on creating a funding policy, which is a best practice, according to the GFOA, that would help contributions remain stable, offset risk, and develop and determine document funding decisions to better manage risk. Much of this info comes from the actuary, legislative directives, and investment policy. Mr. Hole requested the Board to further consider implementing this policy.

Old Business

None.

Ms. Wenguer said the software upgrade is going very well, and the Plan grid is being finalized. She noted it has been very helpful to have Mr. Stanley work with the software provider.

The Board determined that the results of the 2011 Audit and the Actuarial Experience Study would be communicated to the City Commission.

There being no further business to come before the Board at this time, the meeting was adjourned at 5:10 p.m.

Close Window