CITY OF PONTIAC, MICHIGAN
GENERAL EMPLOYEES RETIREMENT SYSTEM
BOARD OF TRUSTEES
MARCH 21, 2012

A regular meeting of the Board of Trustees was held on Wednesday, February 22, 2012 at the City Council Conference Room, Second Floor, City Hall, 47450 Woodward Avenue, Pontiac, Michigan 48342. The meeting was called to order at 1:35 p.m.

TRUSTEES PRESENT	**OTHERS PRESENT**
Shirley Barnett	Matthew Henzi, Sullivan, Ward, Asher & Patton
Koné Bowman *(arr. at 1:37 pm)*	Laurance Gray, Gray & Company
Charlie Harrison, Chairman	Edward Goard, Munder Capital Management
Leon Jukowski, Mayor *(arr. at 1:37 pm)*	James Kelts, Munder Capital Management
Phyllis Long	Ellen Zimmermann, Retirement Administrator
John Naglick, Secretary	Jane Arndt, M- Administrative Assistant
Tuesday Redmond	Larry Marshall, Retiree
Sheryl Stubblefield	Linda Watson, Retiree
Patrice Waterman	
Kevin Williams	

PUBLIC DISCUSSION/UNION REPRESENTATIVES

AGENDA CHANGES

APPROVAL OF CONSENT AGENDA

A. Minutes of Regular Meeting: February 22, 2012
B. Communications
  1. Correspondence from AMBS Re: March Newsletter
  2. Correspondence from Gray & Company Re: Performance Summaries
  3. Correspondence from Kennedy Capital Re: Directed Brokerage
  4. Correspondence from NCPERS Re: Fiduciary Liability Insurance Update
  5. Correspondence from OakBrook Re: Client Letter and Performance Summary
  6. Conference Information
     a. MAPERS Spring Conference – NCPERS – May 20-22, 2012
     b. Washington Legislative Update – IFEBP – May 7-8, 2012
C. Financial Reports
  1. Financial Reports – February 2012
  2. Capital Calls:
  3. Accounts Payable
     a. ADP $8,212.92

b. Arnall, Golden, Gregory LLP 2,381.00
c. City of Pontiac (reimburse 2011 expenses) 151,977.62
d. Coffee Break 35.00
e. Discovery Health Records 70.62
f. GE Capital 116.42
g. Gray & Company 8,104.17
h. Healthport (Sielbeck records) 102.64
i. Office Depot 536.04
j. Rodwan Consulting 1,400.00
k. Slade's Printing 33.60
l. Stevens Records Management 60.72
m. VISA 2,785.79

D. Retirements, Refunds, Final Calculations, Re-Examinations
1. Remove from the Rolls:
   a. Philip Waters (deceased 03-08-12): survivor benefit of $338.19/mo to Helen Waters
   b. Carolyn Denio (Sturdevant) (deceased 02-23-12)
   c. Jane Matthews (deceased 03/01/12)
   d. Terrance McCormick (deceased 02/27/12)
2. Pop-up Effective
3. Application for Service Retirement:
   a. Brigida Cantu – PMEA 7 years, 2 months Age 63 (off def)
   b. Betty Hitchuk – Non Union 16 years, 4 months Age 60
4. Applications for Deferred Retirement:
5. Final Benefit Calculations:
6. Change of Retirement Effective Date:
7. Disability Re-Examinations:

RESOLUTION 12-026 By Williams, Supported by Long
Resolved, That the Board approve the consent agenda for March 21, 2012.

Yeas: 10 – Nays: 0

CONSULTANTS

Re: Gray & Company

<u>Munder Capital – Requested IPS Change for Fixed Income</u>
Mr. Gray indicated that core fixed income represents 9.7% of the plan or $42 million in assets and is managed by Munder Capital Management. The current Investment Policy Statement limits Commercial Mortgage Backed Securities (CMBS) to 2% to 3%. Munder is asking that the percentage be raised to 10%. The Board had questions so they asked that Munder would come in and explain their request.

Mr. Goard stated that the System's portfolio performance to date is up 1.25% and is 50 basis points ahead of the benchmark. At the roundtable session they asked that the Board allow them to take the exposure to CMBS up to 10%. CMBS exposure of around 6% to 7% has been part of their typical core strategy for the past several years. He indicated that underwriting standards are stricter than they were prior to the financial crisis. The deal structure is in high quality properties with less loan to value with plenty of protection to bond holders. They produce better yield and have lower risk than corporate bonds.

James Kelts thanked the Board for the opportunity to speak about commercial mortgages and their focus in the marketplace. He indicated that commercial mortgages produce better income.

Commercial mortgages differ from residential mortgages in size, structure and call feature. They can be valued at several hundred million dollars. They have a shorter life with maturities of five to ten years. They have strong call protection and defeasance with the borrower pledging U.S. government securities which helps to insure that there is more certainty in cash flow and when the money is paid back..

He reviewed the factors used when analyzing a commercial mortgage loan. The debt service covered ratio (DSCR) is the best indicator of default probability.

The lower the loan-to-value (LTV) the better and it equates to more equity in the property.

The term structure determines the length of the loan and whether it is an interest only (which was the problem in 2007) or an amortized loan.

Chairman Harrison asked what the typical loan- to-value is with CMBS and how that equates to risk.

Mr. Kelts explained that the CMBS structure is an individual pool of diversified mortgages that are grouped in tranches from super senior AAA down to non-investment to unrated. As a AAA investor you would be protected by the tranches below you. Thirty percent of the lower tranches have to take the losses. Minimally, 60% of all the loans have to default for the senior tranche to take any losses. Most of these mortgages are super senior grade going down to AS. The average loan-to-value is 60% versus 70% in 2007. There were no defaults in AAA in 2007 through 2008. He is comfortable that the System would not take any credit loss.

Trustee Naglick asked what the credit enhancement is in the senior tranche.

Mr. Kelts stated that it is 10% to 25% off the treasury curve.

Trustee Barnett asked how investors make money.

Mr. Kelts stated that it is based on the principal and interest of the loan. The coupon is currently paying 3.5% and there could be extra carry in the coupon.

Ms. Zimmermann questioned what the AAA default rate is.

Mr. Kelts stated that there has never been a default in AAA.

Mr. Goard stated that most commercial mortgages never take losses. In 2006 and 2007 the lower tranches took losses but AAA did not take losses nor did the bonds take any principal loss.

Mr. Kelts stated that there was a dramatic rise in the issuance of CMBS from 2005 through 2007 due to high investor demand and relaxed underwriting standards. It was much easier then to get a commercial mortgage. It came to a halt in 2008 because no one was lending.

Property valuations mirrored issuances in 2007. Property valuations decreased and there was not enough safety to survive the financial crisis. There has been some modest appreciation in retail and multi-family but you will never see property values at the levels they were prior to the crisis.

Mr. Gray noted an increase from 2010 to 2011 and than a drop off in 2012.

Mr. Kelts indicated that was due to the increased lending standards.

He reviewed the average projected losses in CMBS by vintage year. Projected losses in 2007 are 15% and in 2008 they are 14.8% based on a bear market and 8.8% versus 9.5% in a bull market. Those with a 30% credit enhancement are not expected to take principal losses.

Trustee Stubblefield confirmed that there are going to be losses but based on the investment level the System will not take any losses.

Mr. Kelts compared originations made in 2012 versus those made in 2007. There was an illusion of diversification in the loan detail. The term structure of the loans indicated that 73% of the loans in 2007 were interest only compared to 1.0% in 2012. The top loans in 2007 were 19.0% versus 8.3% in 2012. Anything over 10% eats up the credit enhancement. The higher the debt service the better. In 2007 it was 1.40 versus 1.58 in 2012. Currently the loan-to-value at maturity is 51.2% versus 68.6% in 2007.

He described the CMBS property type mix. Agency-backed CMBS multi-family loan exposure has moved to private label CMBS. CMBS is more skewed to retail loans for newer vintage deals.

The new Barclays AAA rated 2.0 CMBS Index only includes these AAA rated issuances which are what they are currently buying. The spread is much lower than the universe of bonds. A 10% investment in CMBS may seem large but the investment is safer.

Trustee Naglick asked if the ten-year treasury spread is 2.25%.

Mr. Kelts indicated that is the overall spread.

Mr. Goard said that they believe that CMBS is a good investment based on the better underwriting standards, the deal structures have better protection and the yields are better than similar related corporate bonds.

Mr. Gray stated for the record that he agrees that seasoned investment people have trouble predicting rates but they will go up. It is important to let them do everything they can to reduce red ink and lessen negative performance.

Mr. Goard and Mr. Kelts left at 2:08 p.m.

Mr. Gray indicated that there is a firm out of Texas currently at their office talking about the same issue.

Bill Gross from PIMCO was wrong about when interest rates will go up but there is no doubt that rates will go up which will cause bond performance to go down. It would be advisable to give people the latitude and ability for subtle changes to protect the portfolio.

Trustee Naglick stated that at the last meeting it was his impression that these were not high quality bonds and that the manager would be investing in Collateralized Debt Obligations (CDO's) or similar investment vehicles.

Chairman Harrison asked if the Board wants to make this an actionable item and whether the Board had any further questions or concerns.

RESOLUTION 12-027 By Naglick, Supported by Long
Resolved, That the Board approve the amendment to the Investment Policy Statement allowing fixed income to invest up to 10% of their portfolio in Commercial Mortgage Backed Securities (CMBS).

Yeas: 10 – Nays: 0

Flash Report as of February 29, 2012
Mr. Gray provided an overview of the flash report as of February 29, 2012. The total Plan performance for the month is 3.25%. There are a few clean up items including Nexos that needs to be removed from the report.

Ms. Zimmermann indicated that Northern Trust has been notified to record the receipt of assets and remove Nexos.

Mr. Gray stated that last September, 2011 the total Plan value was $378.1 million; at year end it was $403.8 million and as of February 29, 2012 it was $435.6 million.

Total Fund Review
Mr. Gray presented their capital markets observations and a review of the System's asset allocation to the Board.

He pointed out that Chris Kuhn is a budding writer and enjoys writing the capital markets reviews. He feels that it is most important to make the reviews user friendly.

Economic growth is a key factor in the performance of the capital markets going forward. China provides the best prospects with double digit growth but there are concerns with that number coming down. Their current GDP growth is 7.5%. They were a huge user of materials including steel, concrete and building materials but their consumption has declined. Currently, 51% of China's population lives in the City so there is no need to continue building with many of the recently built structures currently empty.

Chairman Harrison asked about the effect of China owning so much U.S. debt going forward.

Mr. Gray stated that China wants to be in control and in the driver's seat. He referred to the sovereign debt crisis in Europe. Countries like Spain, Italy, Greece and Portugal have been living lavish lifestyles. There are concerns that the banks that loaned money to these countries could cause some trickle down effect to China.

The debt burden is rising faster than the GDP in developed countries. People in many of the European countries hate paying taxes and have been borrowing money to pay for their police, road paving and garbage collection. Europe is currently addressing the problem but the United States is not.

In order to see any real economic growth globally, unemployment needs to come down.

The current environment favors emerging countries which are exporters of natural resources and consumer products with a growing middle class. However, issues in China could affect the emerging markets. The frontier nations are where the growth will be including Brazil, Indonesia and South Africa.

Chairman Harrison asked whether there are any developing issues with the U.S. dollar.

Mr. Gray stated that U.S. currency is safer than Japanese currency based on their weak domestic consumption and reliance on exports. There is some offset due to Chinese imports. There has been a bit of a gain injected. The U.S. relies on China buying their debt. The Chinese are buying Treasuries at every auction.

The biggest shock last year was the downgrade of the U.S. bond rating. However, the U.S. is still the safest place to go.

Operation Twist has pushed down long-term rates. Long-term bonds are up almost 29%. Bernanke and company are doing the best they can. He indicated that there has been recent political posturing that somehow the government controls the price of gasoline. He stated that the price of gasoline is controlled by the markets.

The U.S. equity market still has relatively attractive yields. Some investors have allocated more while others are taking their money off the table.

The internationally equity market underperformed in 2011 but is still attractive.

Real estate has not done well. JP Morgan said of real estate that managers buy when there is a lot of blood in the streets, even their own. There was a lot of bad news squeezed out.

When stocks and bonds lag in performance, a number of investors look to private equity and hedge funds. There are a lot of public pension plans choosing these asset classes because they need the returns. This Fund does not have large exposure due to the overfunding.

He compared the target allocation of each asset class to its long-term return assumption. Based on current expectations the current asset allocation policy will exceed the target return assumption with total projected Fund returns of 8.31%.

He indicated that the asset classes are broken down by manager and the amount allocated to each manager.

The First Eagle investment is nearly finalized. They are just waiting on the contracts.

Chairman Harrison asked if the legal work had been completed so the additional allocations can be made to Invesco and Mesirow.

Ms. Zimmermann stated that the Ms. Billings issued a letter regarding Mesirow, however, she has not received the same (PA 314) compliance letter for Invesco.

Their recommendation is to review the fixed income allocation. Currently, 25% of the portfolio is allocated to fixed income. They are already taking steps to insure that these investments are protected from interest rate risk going forward.

Trustee Naglick confirmed that the watch letter had been sent to international equity manager Artio.

He referred to Chairman Harrison's concerns at the last meeting with regard to the GASB proposed reporting changes. These proposed changes could affect the investment rate of return along with the System's funding level.

Mr. Gray stated that the accounting world is sending a message that they want people to stop playing games. They want pension plans to provide holistic reporting.

Chairman Harrison asked what happens if cities are required to contribute and they do not have the funds. Most plans are currently underfunded.

Mr. Gray felt that these plans would be rolled into State plans or require government funding. That is how it is done in the private world.

Chairman Harrison asked how that relates to healthcare funding.

Mr. Gray said that he would have to check with their recently hired actuary and CFA Gregg Johnson. He is reviewing every plan they work with from an actuarial perspective.

He told the Board that they also hired Curtis Spears; Jean Wagley who is a CFA and CPA from Beijing University; Cheyla White who is his new executive assistant and Jennifer Hodges who is in their Chicago Office.

He also indicated that Artio Global Investors has lost $10 billion to $15 billion of their assets. Brigid Flanagan has left and Rebecca Kubick was cut due to the loss of assets.

REPORTS

Re: Chairman
Chairman Harrison told the Board that last year he was recognized by NASP at the State level and now he has been nominated for an award at the national level.

Re: Secretary – None

Re: Trustees/Committees

Personnel Committee
Chairman Harrison indicated that he and Trustee Waterman had a discussion and determined that the Board needs a Personnel Committee now that the employees in the office report to the Board. Trustee Waterman will chair the committee and will chose two other trustees.

Trustee Waterman stated that she will send an email to the trustees and anyone who is interested in being on the committee should contact her.

Ms. Zimmermann asked that the Police & Fire Retirement System Board be included.

Trustee Waterman said that it will be a joint committee. However, she will not wait for them in order to hold a meeting.

Re: Administrator

Payables Information
Ms. Zimmermann indicated that at the last meeting the Board discussed putting all the payables on a single spreadsheet versus individual invoices. She asked for the Board's direction.

RESOLUTION 12-028 By Barnett, Supported by Stubblefield
Resolved, That the Board direct the Administrator to use a spreadsheet to report accounts payables in the consent agenda going forward versus individual invoices.

Yeas: 10 – Nays: 0

Retirement Office Payroll

Ms. Zimmermann reported that at last month's Police & Fire Board meeting they made the suggestion that John Naglick continue to review payroll as an internal control.

<u>Retiree Overpayment</u>
Ms. Zimmermann reported that an overpayment to a member was recently discovered. The overpayment was approximately $9,000.00 and the repayment will be spread out over the beneficiary's lifetime. The beneficiary is in her eighties. The Retirement Coordinator mistakenly picked up the retirement benefit for the member instead of the beneficiary.

Re: Legal

<u>Partial Termination</u>
Mr. Henzi reported that a partial plan termination occurs when there is a 20% loss of members in a retirement system. Since the last meeting he has looked at more information. He may have to go back to 2005 to 2004 to determine if there was a systemic layoff of members that principally started in 2005.

He will work with Ms. Zimmermann to determine which members will become deferred vested. This item is still pending.

<u>Fiduciary Liability Insurance – Deletion of Recourse</u>
Mr. Henzi reported that a waiver of recourse is only used in the private sector. This item is still pending.

<u>Hofmeister Power of Attorney</u>
Mr. Henzi reported that after Ms. Billing's review of the Daniel Hofmeister Power of Attorney there were questions with regard to how the document was executed. A person must be competent in order to sign a power of attorney. Mr. Hofmeister signed the document with an X which brings his competency into question.

Ms. Zimmermann understands Ms. Billing's concerns but feels that Mr. Hofmeister may not have been physically able to sign his name so he signed with an X. She explained that the Retirement Coordinator at the time, Melissa Tetmeyer, went to the hospital on behalf of the member to notarize his retirement documents so they could be processed. Going to the hospital is a rare occurrence. Perhaps Ms. Tetmeyer could sign an affidavit.

Mr. Henzi stated that Ms. Tetmeyer could sign the affidavit as a witness to confirm whether Mr. Hofmeister was competent and understood what he was signing.

Trustee Bowman indicated that the document was not witnessed.

Mr. Henzi indicated that the document being notarized is the same as being witnessed.

Trustee Waterman stated that she knows his wife Mona was there when the document was executed.

Mr. Henzi stated that executing a document with an X for a signature is rare but it does happen. He will work on resolving this issue.

Mesirow Financial Private Equity Partnership Fund VI
Mr. Henzi reported that based on Ms. Billings' review of the Limited Partnership Agreement, the Private Placement Memorandum, the Subscription Agreement and the Form ADV Part 2A it the investment qualifies under Public Act 314.

Robbins Geller Portfolio Monitoring Report 3rd Quarter 2011
Mr. Henzi reported that this is for the trustees' information.

The NAPPA Report, February 2012
Mr. Henzi reported that this is for the trustees' information.

Employee Benefits Legal Blog Settlor vs. Fiduciary Functions
Mr. Henzi reported that this is for the trustees' information.

RESOLUTION 12-029 By Waterman, Supported by Bowman
Resolved, That the Board approve the move to closed session to discuss pending litigation.

Roll Call:

Trustee Barnett – yea	Trustee Naglick - yea
Trustee Bowman – yea	Trustee Redmond – yea
Chairman Harrison – yea	Trustee Stubblefield – yea
Trustee Jukowski – yea	Trustee Waterman - yea
Trustee Long - yea	Trustee Williams - yea

The Board moved to closed session at 2:55 p.m.
Trustee Redmond returned at 2:57 p.m.
Trustee Redmond left at 3:12 p.m.
The Board returned from closed session at 3:13 p.m.
Trustee Waterman left at 3:13 p.m.

RESOLUTION 12-030 By Bowman, Supported by Naglick
Resolved, That the Board approve the closed session minutes from February 22, 2012.

Yeas: 8 – Nays: 0

RESOLUTION 12-031 By Jukowski, Supported by Bowman
Resolved, That the Board ratify the proxy vote in the Delphi Corporation Securities Litigation.

Yeas: 8 – Nays: 0

RESOLUTION 12-032 By Williams, Supported by Bowman
Resolved, That the Board ratify the Chairman's signature on the Health Management Litigation Agreement.

Yeas: 8 – Nays: 0

RESOLUTION 12-033 By Williams, Supported by Bowman
Resolved, That the Board ratify the Secretary's signature on the Quest Software Litigation Agreement.

Yeas: 8 – Nays: 0

Trustee Waterman returned at 3:16 p.m.

UNFINISHED BUSINESS

Re: Citizen Trustee Appointment
Ms. Zimmermann reported that Executive Order S-166 dated March 12, 2012 orders the immediate reappointment of Citizen Trustee Kevin Williams to a term expiring March 31, 2015.

Re: Board Composition
Ms. Zimmermann reported that Executive Order S-165 dated March 1, 2012 orders the immediate amendment of the composition of the General Employees' Retirement System Board of Trustees.

The amendment to the language of Section 3 (e) was changed to read: Three (3) members of the Retirement System one (1) of whom shall be an active member nominated and elected by the active members and two (2) of whom shall be either nominated and elected by either active, deferred vested and retired members (Herein after referred to as the Member Trustees).

Under Section 3 (g) the language was changed to allow for one (1) deferred vested or retired member of the Retirement System who was formerly employed by Pontiac General Hospital to be nominated and elected by the deferred vested and retired members who were formerly employed by Pontiac General Hospital.

Under Section 3 (j) the language was also changed from "the City shall indemnify" to "the Board shall indemnify" to the extent authorized or permitted by law the members of the Board, their representatives, and any other employees of the City who are deemed to be acting on behalf of the Retirement System and hold them harmless, against any and all liabilities, including legal fees and expenses, arising out of any act or omission made or suffered in good faith pursuant to the provisions of the plan, or arising out of any failure to discharge a fiduciary obligation imposed, other than a willful failure to discharge a fiduciary obligation of which the person was aware.

Trustee Barnett asked if the retirees will be notified.

Ms. Zimmermann indicated that the notification will be done as part of the election.

Chairman Harrison asked if the paperwork for the election is included in the agenda.

Ms. Zimmermann indicated that the election information will be brought to the April meeting.

Re: Partial Plan Termination - Refer to Legal

Re: Rent/Overhead
Ms. Zimmermann reported that John Naglick is working with the Emergency Manager to determine the amount of rent to be charged to the systems.

Trustee Naglick indicated that the rent would be $3,500.00 per month. The City formerly allocated overhead of approximately $42,000.00 to the System for the staff. They divided the amount over a twelve-month period which came to $3,500.00.

He also stated that Mr. Schimmel would like to move the staff to a better area of the building. It makes sense that the Retirement Office be moved to where Risk Management is now located. They are looking at a July 1, 2012 date. The delay would be due to the installation of a new phone system.

Trustee Naglick said that the area is approximately 1,500 square feet and that a lot more comes with it than just the space. A better comparable would be a full service office center. He asked how much Mr. Gray is currently paying for his full service office space in the Americenter located at Woodward Avenue and Square Lake Road.

Mr. Gray indicated that he currently pays $1,200.00 per month for an 8' x 8' office for Mr. Kuhn. He also has to pay an additional hourly charge when they rent the conference room. It is his opinion that it would cost the System much more than the $3,500.00 if they relocated outside of City Hall.

Chairman Harrison said if the Board is interested in making changes they should bring information to the April meeting.

Re: Larry Balowski Hearing Request – Refer to Legal

NEW BUSINESS

Re: CPREA Request Regarding Board Composition
Ms. Zimmermann indicated that the letter from CPREA states that they do not want deferred vested members to be eligible due to these members' lack of vesting based on the partial plan termination.

SCHEDULING OF NEXT MEETING

ADJOURNMENT

RESOLUTION 12-034 By Barnett, Supported by Redmond
Resolved, That the meeting be adjourned at 3:28 p.m.

Yeas: 9 – Nays: 0

I certify that the foregoing are the true and correct minutes of the meeting of the General Employees Retirement System held on March 21, 2012

Secretary, John Naglick
As recorded by Jane Arndt