

**CITY OF PONTIAC, MICHIGAN
GENERAL EMPLOYEES RETIREMENT SYSTEM
BOARD OF TRUSTEES
MARCH 7, 2016**

A special meeting of the Board of Trustees was held on Monday, March 7, 2016 at the Retirement Office located at 2201 Auburn Road, Suite B, Auburn Hills, MI 48326. The meeting was called to order at 11:49 a.m.

TRUSTEES PRESENT

Jane Arndt
Koné Bowman
Janice Gaffney
Robert Giddings, Chairman
Walter Moore
Nevrus Nazarko, Secretary
Deirdre Waterman, Mayor

TRUSTEES ABSENT

Sheldon Albritton (*absent*)
Shirley Barnett (*excused*)
Patrice Waterman (*excused*)

OTHERS PRESENT

Cynthia Billings, Sullivan Ward Asher & Patton
Kurt Lofters, Gray & Company (*by telephone*)
Deborah Munson, Interim Executive Director

Chairman Giddings opened the meeting at 11:49 a.m.

PUBLIC COMMENT

AGENDA CHANGES

Ms. Arndt asked the Board to add the NASP annual registration renewal to the agenda. She explained the annual registrations will expire prior to the Board meeting scheduled for March 30, 2016.

RESOLUTION 16-044 By D. Waterman, Supported by Moore

Resolved, That the Board approve the addition of the NASP Annual Membership Renewals to the agenda and the processing of the 2016 Annual Memberships on behalf of the Trustees.

Yeas: 7 – Nays: 0

NEW BUSINESS

Re: Addendum to Amend Investment Consultant RFP

Trustee Moore recommended that the Board approve the Resolution as presented. Marquette Associates is one of the largest investment consulting companies in the country. They do not have any Michigan public funds clients. The Ad Hoc Committee believes it is to the Board's advantage to have the minimum qualifications language requiring respondents to have a Michigan public fund client removed from the RFP.

Chairman Giddings confirmed the language change would be posted on the System's website and in Pensions & Investments magazine.

Trustee Moore added the Board and Committee will still have the authority to choose the Investment Consultant.

Trustee Deirdre Waterman questioned what language is being stricken from the RFP.

The following language is being removed from the minimum qualifications section IV.A.4 and wherever it appears in the RFP "...and one of which must be a Michigan Public Pension Plan."

Trustee Nazarko confirmed no other language in the RFP is being changed.

RESOLUTION 16-045 By Moore, Supported by Gaffney

Resolved, That the Board approves the proposed change to the minimum qualifications section of the Investment Consultant RFP and authorizes the addendum to be added to the RFP immediately.

Yeas: 7 – Nays: 0

Re: Discussion of Portfolio Transition of High Yield Bond Fund to Global Bond Fund

Miss Munson indicated that the meeting was called in order to discuss the transition process from Peritus Asset Management to Brandywine Global. Due to a number of concerns, the process was stopped effective Thursday March 3, 2016 after discussion with members of the Finance Subcommittee. She asked the Board to ratify the Chairman's signature on the Northern Trust Letter of Direction.

RESOLUTION 16-046 By Nazarko, Supported by Gaffney

Resolved, That the Board ratifies the Chairman's signature on the Letter of Direction to Northern Trust.

Yeas: 7 – Nays: 0

She explained there are questions regarding whether the Board approved the transition process, the hiring of Oppenheimer or whether the former Executive Director had the authority to execute the process using her signature authority.

She had also contacted Ron Heller from Peritus Asset Management based on his December 4, 2015 email to Ms. Carter in which he expressed his concern of the prices that Oppenheimer was receiving for the sale of the assets. Mr. Heller indicated in his email that because Oppenheimer was hitting low bids they were eroding the principal in the System's account. Ms. Munson referred to his email and letter included in the agenda. He has offered to provide a reconciliation of the assets, act as a non-discretionary advisor on the remaining assets and provide the Board with a plan of action for the management of the remaining assets. As a high yield manager they understand the market and how to obtain fair market value. Peritus has also indicated they would complete the liquidation process on behalf of the System on a per basis point fee.

Mr. Lofters told the Board that the liquidation had to occur based on the Board's termination of high yield manager Peritus for poor performance. He explained there is no way to directly transition high yield bonds into a global fixed income commingled fund. The high yield bonds had to be liquidated in order for the System to use the cash to buy shares in the commingled fund. The transition manager or execution-only broker would sell the bonds as close to market value as possible. Oppenheimer has done their job. He opined that had Peritus been used for the transition they would have held onto the bonds until the market went up in order to preserve the assets and in order to protect their other investment offerings. He stated that Mr. Gray indicated this is the same process they used for past transitions.

Miss Munson stated in the past the Board approved the transition manager and an agreement was put in place prior to the transition of assets.

Ms. Billings read her legal opinion regarding the transition process and the Interim Executive Director's concerns that the former Executive Director misused her signature authority. The former Executive Director signed and used the System's signature authority resolution that was adopted by the Board on November 30, 2011 to conduct business on behalf of the Board.

The resolution does not authorize specific individuals to have signature authority. The resolution authorizes specific positions, i.e. Chairman, Secretary and Administrator to have signature authority. While not dispositive to the issue, there appears to be support for the fact that the Board did not authorize specific individuals to be authorized signors in certain meeting minutes wherein Ms. Zimmermann advised the Board that the Signature Authority needed to be updated, but a vote was never taken.

She further explained minutes from the February 29, 2009 meeting wherein one Trustee stated "they should postpone this approval (for signature authority) since the Finance Director had not been confirmed." It appears that a vote was never taken to add this specific individual. The minutes from December 2, 2015 Board meeting also states that "the signature authority is based on position not the individual."

It is her opinion that it was appropriate for both Ms. Carter and Mr. Nazarko, on the basis of their respective positions with the System, to provide specimen signatures for the signature authorization.

On April 29, 2015 the Board adopted Resolution 15-024 to authorize the termination of high yield manager Peritus Capital Management and to transfer the assets to an index fund "under the guidance of the Investment Consultant".

On Monday, November 23, 2015 Ms. Carter sent an email to Northern Trust, Brandywine and Peritus regarding the transition of assets. She indicated it is important to note that both Gray & Company and Oppenheimer were copied on the email which in her opinion indicated that Gray & Company was involved in the process as requested by the Board in Resolution 15-024.

Mr. Lofters sent an email to Ms. Carter in response to an email she received from Peritus alleging that Oppenheimer "is dumping the Pontiac securities."

Mr. Lofters stated he spoke with Kathleen Colin at Oppenheimer regarding the allegation. He reviewed the transition from Peritus to Brandywine Global based on sixty-six positions to transition. He indicated that to-date twenty-two full positions and five and a partial positions had been transitioned. He also stated it could take time to sell the positions because the transition manager does not want to sell positions at rock bottom prices.

Ms. Billings again referred to Resolution 15-024, to support the idea that the transition of the assets from Peritus were under the guidance of the Investment Consultant.

She asked Mr. Lofters if it is Gray & Company's position that the Board should follow the recommendation of the investment consultant to continue the liquidation of Peritus assets and move the cash to Brandywine.

Mr. Lofters confirmed that Larry Gray has said he has confidence in Oppenheimer continuing the transition of assets to Brandywine.

Chairman Giddings indicated there was no written agreement in place with Oppenheimer to transition the Peritus assets to Brandywine. Oppenheimer acted as an execution-only broker liquidating the Peritus assets in order to buy into the Brandywine portfolio. To-date approximately \$11 million has been transitioned to Brandywine with a realized loss of \$3.6 million. There is still \$6 million to transition. Based on the lack of an agreement trading was stopped.

Miss Munson reviewed the transition process to date. The Board hired Brandywine as a global fixed income manager in August, 2015. The resolution indicated that the Chairman was authorized to execute the appropriate documents to cause the investment of System assets into the Brandywine Global commingled fund. She cited samples of how transitions were done in the past. The Board has either resolved to allow the current manager to manage the transition (Kennedy Capital 2015); had the current manager liquidate the current portfolio (Artio 2012) or hired a transition manager (Ambassador 2010). The Board did not take any action with respect to the Peritus to Brandywine transition.

In November, 2015 Ms. Carter authorized Oppenheimer to provide "execution-only" services for the transition. The Board never authorized the use of a transition manager or execution-only broker or any other third party to liquidate the assets. There also was no written agreement with Oppenheimer to provide these services. Oppenheimer assumed control of the assets and began the liquidation of the assets based solely on the Direction Letter that was sent to the custodian (Northern Trust.)

In February, 2016 she received a request from Northern Trust for the Chairman to sign a Form 144A allowing the exchange of some private securities held in the Peritus portfolio. At that time she discovered there was no agreement in place with Oppenheimer.

As of November 30, 2015 the cost basis value of the System's portfolio with Peritus was \$23.1 million including cash. The market value of the assets was \$19.4 million. Oppenheimer has sold assets with a cost basis of \$16.6 million. The System received net proceeds of \$13 million. This represents a \$3.6 million realized loss; however the securities that were sold reflected a \$2.9 million unrealized loss as of November 30, 2015 based on statements from Northern Trust. As an execution-

only manager Oppenheimer has no mandate for best execution. She explained the matter to members of the Finance Subcommittee and - based on their consensus - the liquidation was interrupted.

She presented to the Board two options. They can either ratify Ms. Carter's action and have Oppenheimer proceed with the liquidation or they can sign a non-discretionary manager agreement with Peritus who would provide asset reconciliation and oversight until the March 29, 2016 finance sub-committee meeting where Peritus would like to present their plan for either an orderly liquidation or (alternatively) resume active management over the remaining assets.

Ms. Billings told the Board that by not following the Investment Consultant's recommendation they could be liable for the performance of the assets.

Trustee Moore expressed his concerns with regard to Peritus and asked why the Board would use a manager they have terminated.

Trustee Deirdre Waterman confirmed the Investment Consultant has recommended the continuation of the Oppenheimer liquidation. She confirmed the former Executive Director and Investment Consultant entered into the process with Oppenheimer.

Trustee Bowman confirmed with the Investment Consultant that the Board's only option was to liquidate the Peritus assets in order to move them to Brandywine.

Trustee Deirdre Waterman questioned how Oppenheimer was engaged.

Miss Munson told the Board the former Executive Director engaged Oppenheimer indirectly through a direction letter to Northern Trust.

Ms. Billings indicated the engagement process was covered in her legal opinion. The former Executive Director used the blanket signature authority to transition the assets from Peritus to Brandywine referring to Resolution 11-115 in her legal opinion. The broker was obtained from the directed brokerage list which she said had been done in the past per the Investment Consultant.

Miss Munson pointed out that Larry Gray was incorrect when he indicated that the past practice was to use the directed brokerage list to determine which broker to use when transitioning assets. She continued that the Trustees had in the past approved by resolution the firm and transition method.

Chairman Giddings explained the Finance Committee's position for stopping the transition. The Board would like to move forward by redefining the process and having an agreement in place.

Trustee Nazarko stated said that the blanket signature authority does not give him the authority to execute transactions on behalf of the Board but only to ratify with his signature what has been authorized by the Board. He stated that the Board should not confuse having signature authority with execution ability. He is concerned with the disposal of the assets. He feels that Oppenheimer traded the securities illegally.

Trustee Moore questioned why Trustee Nazarko would consider the transition illegal.

Trustee Nazarko indicated the transition was illegal because the Executive Director did not receive approval from the Board to engage Oppenheimer to execute the liquidation of the assets.

Trustee Deirdre Waterman asked Mr. Lofters for his role in moving the assets from Peritus to Brandywine.

Mr. Lofters described the process and when he became involved. He again indicated that the Peritus assets would have to be liquidated in order to move them into the Brandywine commingled fund.

He further explained that the Peritus portfolio has lost 18% (as of November 30, 2016). He explained the current situation in the high yield market indicating that oil prices have impacted the Peritus portfolio. The only way to avoid losses would be to stay in the high yield market and wait for it to come back in favor. Peritus has a conflict of interest with regard to managing those assets for the System.

Trustee Deirdre Waterman confirmed Mr. Lofters was not involved in the original process. She also asked what his recommendation would have been if he was involved early on in the process.

Mr. Lofters said there is a good chance the market would have continued to decline in high yield.

Trustee Bowman confirmed that Mr. Lofters is recommending a liquidation manager versus a transition manager.

Mr. Lofters stated a transition manager is used when you are moving securities in the same asset class. In this case there is no need for a transition manager because the assets are moving into a different investment vehicle. He believes that Oppenheimer's only job is to get fair prices for the assets.

Trustee Nazarko indicated it is the Consultant's responsibility to determine if Oppenheimer is dumping bonds.

Trustee Deirdre Waterman expressed her concern that no one is looking out for the Fund's best interest.

Trustee Gaffney noted the Trustees are spending time trying to lay blame. The Board needs to determine how to move forward.

Trustee Nazarko questioned why it took so long for the assets to be transitioned from Peritus when the Board voted in April 2015 to move the assets into an index fund especially when the high yield market performance was steadily declining.

There was Board discussion whether the Investment Consultant waited too long to transition the assets out of Peritus since the manager was terminated in April, 2015.

There was also discussion regarding how to move forward with transferring the assets to the Brandywine portfolio including hiring a third party to look at the information.

Mr. Lofters recommended the Board should sit down with Oppenheimer to address the issues.

Trustee Moore asked why the Board would use Peritus questioning the fact that they put equities in their portfolio.

Miss Munson confirmed with Mr. Lofters that Gray & Company could obtain a summary of the trades that would include the bid/ask information when the trade was executed for the Board.

Mr. Lofters again stated it would be best to get Oppenheimer in front of the Board. The only information indicating that assets were being dumped came from Peritus.

Trustee Moore asked what the Board should do in the interim with the \$6 million left in the Peritus portfolio.

Trustee Deirdre Waterman questioned why it took so long to move the assets out of the Peritus portfolio and requested a timeline from the Investment Consultant.

Ms. Billings stated the Investment Consultant has indicated they will provide a timeline.

Chairman Giddings stated the Board needs to put a written agreement in place before transitioning the remainder of the assets.

Trustee Gaffney said the Board should not preclude an investigation of the liquidation of assets.

Chairman Giddings stated he has spoken with Larry Gray on looking into another broker to complete the process.

Trustee Moore recommended staying with Oppenheimer to complete the transition.

Trustee Nazarko again noted that the high yield market has a limited number of buyers and smaller trades. He is concerned that the System has lost assets and will lose more assets in the liquidation by continuing with Oppenheimer.

Trustee Dierdre Waterman suggested looking into the various options including having Oppenheimer or another broker continue the liquidation as well as hearing the Peritus presentation on their proposed options.

RESOLUTION 16-047 By Nazarko, Supported by Gaffney
Resolved, That the Board authorizes the Executive Director to wire the current cash balance in the Peritus account to Brandywine.

Yeas: 7 – Nays: 0

RESOLUTION 16-048 By Nazarko, Supported by Gaffney
Resolved, That the Board authorizes the continuation of the liquidation of the remaining assets in the Peritus account assuming a retainer agreement can be executed with Oppenheimer or one of the other brokers on the directed brokerage firm list or another qualified firm.

Yeas: 6 – Nays: 1 (Nazarko)

SCHEDULING OF NEXT MEETING/ADJOURNMENT

Regular Meeting: Wednesday, March 30, 2016 at 10:00 a.m. – Retirement Office

RESOLUTION 16-049 By Bowman, Supported by Waterman
Resolved, That the meeting of the Board of Trustees of the City of Pontiac General Employees' Retirement System be adjourned at 1:49 p.m.

Yeas: 6 – Nays: 0

I certify that the foregoing are the true and correct minutes of the special meeting of the General Employees Retirement System held on March 7, 2016

As recorded by Jane Arndt