

**CITY OF PONTIAC, MICHIGAN
GENERAL EMPLOYEES RETIREMENT SYSTEM
BOARD OF TRUSTEES
December 14, 2018**

A meeting of the Board of Trustees was held on Friday, December 14, 2018 at the Pontiac General Employees' Retirement System Office located at 2201 Auburn Road, Suite B, Auburn Hills, Michigan 48326. The meeting was called to order at 1:00 P.M.

TRUSTEES PRESENT

Sheldon Albritton, Vice Chair
Chad Chandler (telephonically)
Janice Gaffney (arrived at 1:05 p.m.)
Robert Giddings
Walter Moore, Chairman
Billie Swazer
James Walker (telephonically)
John White

OTHERS PRESENT

Cynthia Billings-Dunn, Sullivan, Ward, Asher & Patton
Deborah Munson, Executive Director
Kristy Neumann, Executive Assistant
David Lee, Dahab & Associates (telephonically)
Steven Roth, Dahab & Associates (telephonically)
Linda Watson, City Retiree
Jane Arndt, City Retiree

TRUSTEES ABSENT

Deirdre Waterman, Mayor (excused)
Patrice Waterman, City Council (excused)

Chairman Moore opened the meeting at 1:00 p.m.

PUBLIC COMMENT –

Retiree Linda Watson asked why the Board chose index funds. Chairman Moore responded that everything applicable will be explained and instead of trying to repeat things it would be best to just discuss it later on according to the agenda.

AGENDA CHANGES

Chairman Moore indicated he would just like to add to the agenda for further discussion the Board's consideration to attend a NCPERS Legislative Conference in Washington D.C in January 2019.

CONSULTANTS –

Kennedy Capital Staff Changes

Mr. Roth stated that Kennedy Capital contacted Dahab and Associates on December 4, 2018 to notify them that the two-person management team (John Rackers and Chad Hoffman) of the small-cap growth portfolio had left Kennedy Capital. He reminded the Board that these two joined Kennedy in 2014 and that the GERS was one of the first investors in the small-cap growth product they oversaw. Kennedy Capital hired a new CEO approximately a year and half ago who was going to come in and help grow the firm. That CEO left within this past year. After the departure of the CEO, the two portfolios left to join WCM. It is not uncommon for portfolio managers to pursue other opportunities and – as long as there is a succession plan and a continuation of the investment philosophy – Dahab is comfortable with it. But when the two lead decision-makers leave suddenly, this gives Dahab pause. The question

they ask is would they hire this firm today. Since there is no succession plan and they are not familiar with the track record of the new portfolio manager, there could be changes to the investment process and/or philosophy. Because of that, Dahab is recommending that the Board move these assets into an index fund.

Mr. Roth explained that an index fund is a passively managed fund which tracks a particular index. The System can maintain its exposure to the small-cap growth asset class while the Board considers the alternatives. He reminded the Board that a part of the next steps of the rebalancing process is to look at the Emerging Manager Program to determine whether it will remain solely large-cap or whether to have emerging managers investing in all the asset classes. If the Emerging Managers are going to compete in all the asset classes, transferring the assets to an index fund is a good temporary transition.

Trustee Albritton asked how the Northern Trust index fund was selected.

Mr. Roth responded that it was a matter of what most convenient and least expensive. He said that there is little difference among index funds with respect to the fees and the tracking error. The Board has an existing relationship with Northern Trust and to amend the agreement was relatively cheap and – since Northern Trust is the custodian – it is an efficient process to move the funds short-term. The cost of the index fund is 6 bps and active management costs 75 – 90 bps. Kennedy charges 85 bps. It may be possible to find an index fund with another company for 5 bps but the legal fees incurred in the contract review would offset any savings.

Miss Munson added that another factor that went into the selection of Northern Trust is the savings on the commission costs. Northern Trust would charge a commission of \$.01/share. If the Board decides to go another route, we would need to engage the services of a transition manager. She reiterated that this is the most expedient solution. Index funds have daily liquidity. If the Board wanted to come back in a few weeks after Dahab has had an opportunity to review other index funds, the Board could make a change at that time and there are no additional trading costs.

Ms. Billings-Dunn added that the Board hired Kennedy Capital and those two portfolio managers to manage the assets. Those two people are now gone and the System now has a portfolio manager who the consultant does not have enough information to know whether they can or will manage the assets in the same fashion.

Trustee White asked whether this is normal process that we follow in these situations and whether any other index fund was considered.

Miss Munson responded that this it is a rare occurrence for the lead managers to resign suddenly at the same time with no succession plan. She explained that the Board hires the consultant to help with these decisions. The consultant is advising that they believe it is prudent to move the assets at this time. This is the process we follow under these circumstances like this where the two main decision-makers have already left the firm. No other index was considered because all of the index funds are

the same and hold the same stocks. The advantage that the System would have with Northern Trust is the reduced cost and ease of transition. Northern Trust lowered their management fee on this index fund from 8 bps to 6 bps because of the existing relationship.

Trustee Walker stated that Dahab has done what we hired them to do and erring on the side of caution is the proper thing. Since the two managers who we hired are gone, he believes it is prudent to reinvest the portfolio elsewhere and make an informed decision going forward.

Trustee Gaffney stated that we do not owe anything to any of the investment managers. The people that we owe loyalty to are the retirees and we need to do what is best for them. The consultant is advising that the safest thing to do right now is to put it in an index fund.

Trustee Giddings remarked that in 2014 Kennedy came to us with the new product for the small growth fund and now that the two managers are gone, it is a different situation and that there was no loyalty to Kennedy at this time.

Ms. Billings-Dunn asked whether the index funds of the same asset class from different firms are similar and whether Dahab could bring a search report to the January meeting.

Mr. Roth explained that the returns and the fees of the various index funds will be roughly the same. The only thing that will vary is the documentation. He said that Dahab could put a search together but it would not be in January because it requires posting for a certain period of time. He noted that the more pressing issue is deciding what to do with respect to the emerging managers and whether we would allow them to participate in all the asset classes. That will dictate a lot of the underlying pieces.

Trustee Swazer asked why the Northern Trust Emerging Markets Index is referenced in the documents.

Miss Munson responded that one of the benefits of selecting Northern Trust is that the System would not have to go through the process of a legal review of an investment agreement. If Northern Trust is selected, we will not have to sign a new agreement. The agreement that the System has with Northern Trust for the Emerging Markets Index Fund would be amended to add the Small Cap Growth Index Fund. This is why the document lists both Funds.

Trustee Swazer asked what are the returns of the Northern Trust Small Cap Growth Index Fund.

Miss Munson responded that the 10-year return for the Northern Trust Small Cap Growth Index Fund is 10.94% versus the Russell 2000 index of 11.11%.

Mr. Roth responded that it was December and – yes - we would react or make the same recommendation with other managers if such a big change were to occur but if it were a normal situation such as a manager retiring etc., and the transition was planned and smooth then no we would not.

Chairman Moore responded that this was all the more reason that we need to educate ourselves and take this opportunity to learn about Index Funds and if we can reduce basis points and fees the Board would be doing an injustice not to at least investigate it further

Trustee Giddings asked whether every share in the portfolio had to be liquidated since a lot of the holdings should be the same as the index fund.

Miss Munson responded that she did ask Northern Trust whether they could take some or all of the assets in-kind into the Fund. Northern Trust said that they could not because the size of our positions was too small to be transferred in efficiently.

Chairman Moore commented that he has been reading a lot regarding the market and investments and that future prediction indicate that the majority of people will be switching to Index Funds because of the high management fees and it's imperative that we have more information we educate ourselves. He said that we only need to make 7%, and if we are hitting the 7% with the Index Fund and also saving on the fees, the Board should consider that.

Trustee Gaffney remarked that some assets are fine with no management and some might require a little more management and was inclined to agree with Chairman Moore's philosophy.

Trustee Giddings stated that he agrees with the idea that this is just temporary and the time is needed to perform our due diligence, but asked if we move the assets to Northern Trust, how much of the portfolio are they managing?

Mr. Roth replied about 5%.

David Lee joined the call at 1:45 p.m.

Trustee Albritton commented that he agreed that a decision needed to be made and moving forward with Northern Trust made sense but stressed his feelings about the importance of having a timeframe to present some new managers so nothing goes stagnant and/or forgotten about and suggested the end of the first quarter of 2019.

Chairman Moore said he was less concerned with the search for a new manager and felt it was more important to have some education and training on index funds and once we are more educated we can make a better decision moving forward.

Chairman Moore stated that this was another example of why he wanted to have an educational retreat to discuss this as well as other things.

Trustee Gaffney stated that she felt that the training and education should be the first priority and then a timeline can be established. We don't want to hire an active manager before we have the training and deal with the emerging managers and then come back afterwards and think we should have made a different decision.

Chairman Moore asked Dahab if they will be able to provide the education and training regarding Index Funds including fees.

Mr. Lee commented that they would and that they would accommodate the schedule of the Board.

Chairman Moore asked Mr. Lee to send some dates to Miss Munson.

RESOLUTION 18-148 By Gaffney, Supported by Giddings

Resolved, That the Board approved to terminate the Kennedy small cap growth account and, further

Resolved, That the Board approves to employ Northern Trust Investments, Inc. to liquidate the assets in the Kennedy small cap growth account and transfer the proceeds to purchase shares in the Northern Trust Collective Russell 2000 Growth Index Fund – Non-Lending, and, further

Resolved, That the Board authorizes the Chair and the Executive Director to execute the necessary documents to effect this transaction, subject to legal review of the same.

Roll Call:

Albritton - Nay
Moore - Yea

Chandler – Yea Swazer - Nay

Gaffney – Yea Walker - Yea

Giddings – Yea White - Yea

RESOLUTION 18-149 By Gaffney, Supported by Albritton

Resolved, That the Board approves attendance for all interested Trustees at the NCPERS Legislative Conference being held in Washington, D.C.

Yeas: 8 – Nays: 0

SCHEDULING OF NEXT MEETING

Regular Meeting: Wednesday, January 30, 2019

RESOLUTION 18-150 By Gaffney, Supported by Albritton

Resolved, That the meeting of the Board of Trustees of the Pontiac General Employees' Retirement System be adjourned at 2:17 p.m.

General Employees' Retirement System
Special Meeting
December 14, 2018

Yeas: 8 – Nays: 0

I certify that the foregoing are the true and correct minutes of the meeting of the General Employees Retirement System held on December 14, 2018

As recorded by Kristy Neumann, reviewed and edited by Legal Counsel and Executive Director