MINUTES
GENERAL EMPLOYEES' PENSION BOARD
POLICE OFFICERS' PENSION BOARD
FIREFIGHTERS' PENSION BOARD
HELD AT CITY HALL

May 15, 2015	**8:30 a.m.**	**Commission Conference Room**

1. CALL TO ORDER

Chairman Kelly McGuire called the meeting to order at 8:35 a.m.

General Employees' Pension Board members present were Chairman Kelly McGuire, Michael Furman, and Scott Selis.

Police Officers' Pension Board members present were Chairman Ken Artin, Secretary Shane Jarrell, Amanda Hayes, and Royce James.

Firefighters' Pension Board members present were Chairman Joe Dupree, Secretary Dominic Morgese, Tommy Bozeman, and Brian Daly.

Also present were Mark Harrell of Apex Capital Management, Scott Mullet of GW Capital, Inc., Lee Dehner of Christiansen & Dehner, Charles Mulfinger and Scott Owens of Graystone Consulting, and Patrick Donlan of Foster & Foster.

2. APPROVAL OF MINUTES OF FEBRUARY 13, 2015

Mr. Scott Selis moved, seconded by Mr. Michael Furman, to approve the minutes of the February 13, 2015, meeting. The motion passed unanimously.

Ms. Amanda Hayes moved, seconded by Mr. Royce James, to approve the minutes of the February 13, 2015, meeting. The motion passed unanimously.

Mr. Brian Daly moved, seconded by Mr. Tommy Bozeman, to approve the minutes of the February 13, 2015, meeting. The motion passed unanimously.

3. PUBLIC COMMENT

There were no public comments.

4. ELECTION OF FIFTH TRUSTEE

Ms. Amanda Hayes proposed Dr. Andrew Harris as Fifth Trustee. She stated that he was a chiropractor who had recently moved to this area and desires to serve on the board.

Ms. Amanda Hayes moved, seconded by Mr. Shane Jarrell, to elect Dr. Andrew Harris as Fifth Trustee of the Police Officer's Pension Board to serve a two-year term to March 1, 2017.

5. PRESENTATION OF APEX CAPITAL MANAGEMENT (Small/Mid Cap Growth)

Mr. Mark Harrell stated he was in charge of Business Development and Client Portfolio Manager. He stated they were hired last year and he believed received funding on January 8, 2015. He stated he would refresh us on the firm, process and philosophy and then walk through performance since inception.

<u>Firm</u>
He stated Apex was based in Ohio (i.e., the wall street of the mid-west) and had been in business since 1987. He stated they were founded by Nitin Kumbhani, Chief Investment Officer of Apex, who came to the United States from India for his education. He stated Mr. Kumbhani worked his way through grad school in electrical engineering and computer software, and then founded a software firm. He stated he was one of the pioneers that developed the software that drove ATM machines, which was why they were based in Dayton, Ohio, which was the backbone of the ATM business in the 70's and 80's. He noted that NCR was headquartered in Dayton and DieBold in Canton, Ohio. He stated in 1987, Mr. Kumbhani sold his software firm to a larger entity and turned his attention to this business. He stated that there was not as big of a leap from electrical engineering and computer software development to active management, if you grew up in the business. He stated his father was a large commodities trader in India and his mother's family owned one of the oldest brokerage firms. He stated Mr.Kumbhani's passion for this business was kindled at an early age.

Mr. Harrell stated all Apex did was growth investing, up and down the market cap--small cap, smid, mid, all cap, and large cap. He stated that 65% of their assets were institutional and 35% were high net worth.

Mr. Harrell stated they had $6.5 billion under management. He stated their smid portfolio was their largest portfolio and the same portfolio our plans were in.

Process

He stated the investment team was charged with all buy, sell and portfolio construction decisions. He stated they had never lost anyone off of the investment committee and every member of the team was an owner in the firm. He stated that the newest addition to the team, Sunil Reddy, joined the team almost eight years ago. He noted that the philosophy and process had not changed much since the inception of the firm, which was a combination of top down/bottom up investment process. He stated that the top down was not macular economic forecasting but was secular trend identification. He stated they attempted to find companies from the bottom up that met their criteria but within industries and sectors that would benefit from tailwinds provided by secular pockets of growth.

Mr. Harrell stated that they looked for growth companies first and foremost. He stated they reviewed the top third of companies by sector for revenue growth, by EPS growth, companies exhibiting an element of strength, and companies with consistency of earnings for shared growth. He stated that once they had separated growth companies (companies they thought were growing faster than the market) vs. the companies they did not want to spend much time looking at, they turned to identifying improvements and fundamentals by looking at balance sheets and income statements. He stated that it was at this level they were looking for two distinct types of companies, stable growth and emerging growth. He stated that stable growth companies were companies that had solid top line revenue growth with good bottom line in escrow and had consistency of EPS growth. He stated they would be less volatile in difficult environments. He stated that emerging growth was at the other end of the spectrum and were companies that had explosive revenue growth and may not have any earnings for shared growth yet. He stated they were the disrupters that changed the way business was done in the history of the sector, and the revenue growth was explosive but the earnings to shared growth were in the early stages of growth (spending in R&D, infrastructure, sales).

Mr. Harrell stated they constructed the portfolio to be a combination of stable growth and emerging growth. He stated currently 70% of the portfolio was in stable growth companies and 30% in emerging growth. He stated that the most we would see them in stable growth was 80% and the least was 60%. He stated they did not wish to get carried away with emerging growth because it was more volatile. He stated the portfolio was crafted to smooth out the volatility as best they could through different levers they could pull. He stated they could adjust the stable growth to emerging growth and wanted to tilt the portfolio to secular pockets of growth. He noted the secular trends in place were cloud computing, e-commerce, payments and processing, consumer trends, lifestyle, healthcare trends, as well as industrial trends of energy independence, global growth, etc.

Mr. Harrell stated they would rather buy good stocks in sectors or industries that were growing rather than buy a terrific company in a poor sector or industry. He stated they wanted stocks with a tailwind that provided sustainability of the earning streams of the companies they owned.

Sell Discipline

Mr. Harrell stated that they spent as much time identifying candidates to be sold out of the portfolio as they did on candidates to be purchased. He stated the four steps were 1) Price increase. He stated they did not ever let a name become more than 5% of the portfolio, usually at 3.5% was when they started to trim back from a risk control standpoint. He stated they did not want an individual name to be too big of a component to the rest of the portfolio; 2) Price decline. He stated as the growth plateau was starting to rollover, they looked for better opportunities; 3) Swap securities; 4) Stock performance measured vs. Russell 2500 Growth. He stated that they measured every stock's performance to its benchmark over a rolling four-quarter basis. He stated that if a company fell in the lowest two deciles, it was an automatic review and either a sell or an add. He stated that this kept the portfolio fresh and kept them from holding on to a name and riding it all the way to the ground, and it kept an analyst from falling in love with the name he/she authored.

Historical Performance

Mr. Harrell stated that this portfolio had been around since 2000 and performance had been very consistent. He stated that the year-to-date and one-year returns were behind, but longer term performance had been very strong. He stated that their institutional clients (like us) liked to look at performance over a rolling three-year basis. He stated every three-year period by quarter since inception of the portfolio they had outperformed the benchmark (Russell 2500 Growth) 47 out of 49 rolling three-year periods. He reiterated that consistency was there which was driven by a combination of a secular tailwind, as well as stable growth and emerging growth.

Mr. Harrell stated that the return for the quarter was 5.52% vs. the benchmark at 9.51%. He stated the sectors that were the underperformers were Technology and Healthcare. In the Healthcare sector, he stated that Enanta (Hepatitis C drug) and Insulet (diabetes company that made insulin pumps) were weak in the quarter, but both had turned around meaningfully since the end of the quarter. In the Technology sector, he stated that they owned a number of names that were weak in the quarter that were involved in e-commerce. He stated Bitauto Holdings was a Chinese on-line auto trading company that had weak earnings and was hurt by the strengthening dollar, and YY Inc. was another Chinese company that was weak in the quarter, but since the end of the quarter they had rebounded meaningfully and more so through May 15, as they were up 6.13% with the benchmark at 6.69%. He stated the drivers for the outperformance were the names that were weak in the first quarter. He stated that Bitauto was up 25% in the second quarter and YY was up 25% in the second quarter, and Enanta was up 22%. He stated that there had been a rebound in the names that hurt them in the first quarter. He stated they were confident of those names and would continue to hold them, as well as some new names they had bought recently.

Mr. Harrell stated that there was a new theme in security. He stated that Fortinet, Infinera Corporation and FireEye were involved in the security component of cloud computing. He stated that security was critical to governments, corporations and individuals. He stated that these three companies had strong revenue and earnings and they expected them to do very well. He stated they had also purchased MercadoLibre and IMAX. He stated they sold United Rentals, Albermarle, Yelp, and Zulily during the quarter.

Mr. Harrell stated that Consumer Discretionary and Technology were the sectors that were meaningfully overweight. He stated they were underweight in Industrials, slightly underweight in Energy and Materials, and were moving more toward an overweight in Healthcare. He noted that people were throwing money at companies in the bio-tech space and they preferred to invest in companies in the bio-tech space that had drugs in clinical trials that were fairly far down the pipe, such as Phase 1, 2 or 3. He stated that the FDA was fast-tracking companies for their drugs more so than ever, but they had seen significant money thrown at companies with drugs that were not even in clinical trials, or ones in Phase 1. He stated there was such an euphoria of thinking that all these small bio-tech companies could be purchased, which he stated would not be the case. He stated that valuations had gotten extreme and fundamentals had not kept up with the valuations, so they were trying to be careful in the bio-tech space. He stated that was one of the reasons they were down a little bit in the first quarter because the bio-tech space was on fire. He stated they did hold a number of bio-tech companies, but they were ones with a much better shot at getting their drugs approved.

Ms. Amanda Hayes asked if they would dial down their weighting; whereby, Mr. Harrell stated that they had not dialed down at 21%. He stated they held a number of clinical research organizations who helped drug companies get through the FDA process and who made money by helping these drug companies get through the clinical trials by helping them with the clinical studies, software to track the clinical trials, etc. He stated they made money no matter whether the drug made it through the pipeline or not. He stated they felt this was a safer way to go. He stated they held a very small percentage of the drug companies themselves because they were binary, either getting approved or not.

Mr. Harrell stated that they had made meaningful progress vs. the benchmark. He stated that in April they were down 0.1% with the benchmark down 2.08%, and they were up so far in May, as well.

Mr. Dominic Morgese asked if the Enanta drug for Hepatitis C was the one that cost over $100,000; whereby, Mr. Harrell stated that Enanta was not one of those, but unfortunately a lot of those drugs cost $250,000 to $300,000. He stated that the FDA/companies were fast-tracking drugs for rare diseases that there was no cure for.

6. PRESENTATION OF GW CAPITAL, INC. (Small/Mid Cap Value)

Mr. Scott Mullet with GW Capital was present today. He stated that this was the worst report that he had had to give as it had been a very challenging year for them in terms of returns vs. the benchmark.

Mr. Mullet stated that there were no changes in terms of staffing, ownership, or their product line up. He stated they had about $3 billion in assets under management. He stated that there was nothing organizationally different, except the value style was not in favor at this time. He stated that the portfolio at -0.17% vs. 6.58% was almost 700 bps. behind the benchmark for the one-year return, which dragged their three-year and five-year numbers below the benchmark, but since inception they were still ahead of the benchmark at 17.05% vs. 15.75%.

Mr. Mullet stated that the portfolio outperformed for 13 quarters, but also underperformed 13 quarters. Historically, he stated they were still up more than down even though on a quarterly basis they were about equal, but they had more up quarters in terms of outperformance.

<u>Negative Contributors</u>
Mr. Mullet stated the primary area was in Financials, particularly Genworth Financials, Inc. He stated that Genworth was almost a third of what they were down. He stated that they had held Genworth for over three years and still held it.

Ms. Hayes asked if Genworth was a large cap company; whereby, Mr. Mullet stated that it was not, as it was about a $4 billion market cap company.

Mr. Mullet stated that they did not like to own more than 25% in any one market sector. He stated it was their underweight in Financials and Consumer Discretionary and their issue selection in those sectors that hurt them. He stated that Energy was overweight, which also hurt the portfolio. He stated they were focusing on issue selection, Genworth being number one. He discussed Genworth's issues stating that long term they believed Genworth would be a good stock for them to continue to hold.

Mr. Joe Dupree asked when GW would look at a stock for sale; whereby, Mr. Mullet stated that they had low turnover, and tended to buy companies when they felt there was good value, and rode with them until they believed the valuation was a full metric.

Mr. Mullet stated that Tidewater Inc. was the worst performer in the first quarter of 2015 and was the best performer in the second quarter so far to date. He stated that Owens Illinois, also a poor performer, just came out that they were buying another company and their stock was up 10-12% a couple of days ago. He stated they felt the way to get out of the doldrums they were in was by the companies that they currently owned, as a lot of the companies that went down, the valuation was there and would come back for them.

Regarding mortgage insurance, Mr. Scott Selis asked about Genworth and PMI since the boom and the effect it would have on Genworth; whereby, Mr. Mullet stated that he believed it kept Genworth from being as strong as it was in the boom, but it was still in a positive phase in that regard. He stated that for Genworth a key was that housing values were stable to up.

Regarding long-term care insurance, Mr. Selis asked about the demographics (i.e., people living longer) and how it would affect the ultimate liability Genworth would have; whereby, Ms. Hayes stated that those people would receive notification that their premiums were being raised significantly. Mr. Mullet noted that there was pricing power in this space that had not been there for a long time.

Ms. Hayes and Mr. Selis expressed concern about the issues with Genworth; whereby, Mr. Mullet stated that they believed the market was overly discounting a lot of the issues and that was why they saw value in this stock at these levels.

Mr. Charles Mulfinger, Graystone Consulting, stated that in the case of Genworth, whenever they were writing policies and taking premiums, the money normally sat in fixed income and one of the areas they made their return on was how that money was invested until it was paid out. He stated if they were in an artificially low interest-rate environment, they were taking away all the potential earnings that historically they were able to have on reserve. He stated that if rates started to rise, which would eventually happen, it should add a lot of potential earnings on the balance sheet on the existing money they were sitting on.

For the past year, Mr. Mullet stated the largest change in the portfolio had been a reduction in Energy, unfortunately, they did not foresee the massive drop in oil pricing. He stated they believed they were in a different environment for Energy now, so they had pruned back to the point where they had roughly a 5% weighting vs. the market at 4%, which was pretty much a market weight in terms of their Energy exposure. He stated they believed eventually the Energy space would be a great space to invest in and they had held 15-20% of the portfolio in Energy in the past, but they felt that right now was not the time to be jumping into Energy.

<u>High Yield Spreads</u>
Mr. Mullet stated that High Yield and BBB Corporate bonds spreads vs. Treasuries was driven by the trouble in the Energy market. He stated that when spreads were low or declining was usually very positive for the small to smid cap space because a lot of the companies relied on debt to keep their financing going. He stated a lot of the rise was due to Energy. He stated they were still well below historical averages, but there was some caution in terms of what the high yield market was telling them.

Ms. Hayes asked if GW's opinion was a continued steepening of the curve; whereby, Mr. Mullet stated they believed they would see a little more steepening until the Fed got more aggressive and then we would see the short term jump up a little bit, but right now the bond market was telling them that there was a little inflation and economic recovery, so the long end of the curve was starting to come back a little bit. He stated a little bit was 2.2% on a ten-year Treasury. He stated their bond portfolios were basically durational so they were not calling for a massive rise/decline in rates at this time, but they did believe the bias was more towards an upward trend. He noted they thought that last year and were completely wrong, as all rates did was go down last year.

Mr. Mullet stated they had been through a bad period of time before, but they expected the portfolio to turn around in the near future.

7. INVESTMENT MONITOR REPORT (GRAYSTONE CONSULTING)

Mr. Charles Mulfinger, Graystone Consulting, stated the quarter was a difficult quarter for our U.S. equity managers, as they underperformed relative to the benchmark. He stated the international managers outperformed.

Because of the underperformance, Mr. Mulfinger stated he and Mr. Scott Owens contacted the investment managers to see how they were doing in April. He stated they were finding that the managers who did not perform as well in January, February and March bounced back the most in April and May. He stated they actually made up all their underperformance. He stated he was glad to hear Apex, who was a more aggressive, small-cap growth manager, in the short period of time we have had them, had underperformed by a fairly large amount (3.0%), but since then they had made up the 3.0% in the months of April and May. He stated he also contacted HGK, who had said they were going to add to Energy, which hurt them in January and March, but since March Energy had rebounded, so they were up over the benchmark by 300 bps. in the month of April and first part of May.

Mr. Mulfinger stated that they had the most concern with the two managers that performed the worst, HGK and Apex, and both had rebounded, so next quarter should be good if the market stayed like this, as it was very volatile.

Mr. Mulfinger stated that GW also had a heavier weight in Energy, which impacted their return. He stated that GW was theme based and looked at the economy and sectors, then picked the stocks. Historically, he stated they had time periods when they had underperformed and time periods when they had strong performance. He stated the boards went into the small-mid cap area when the market was on the bottom in 2008 and then there was a huge movement up as the market rebounded, which was when we saw relative outperformance short term, which was what we should see. He stated that he had to look at a market cycle (up and down times) when he evaluated a manager. He stated for the past five years the market had only been up markets and the down market occurred seven years ago. He stated that GW actually did outperform for the whole time period and they did as expected top down. He stated that since three managers underperformed, he wanted to start out by explaining the above.

Economy and Market

Ms. Scott Owens stated that there had been a lot of volatility in the market and interest rates. He noted the market was up over 190 yesterday, and managers that underperformed in the first quarter were now almost caught back up. He stated this was an underlying theme for a quarter. He stated that the first quarter of this year was similar to the first quarter of last year as GDP growth was about 1.0% and was revised to several different numbers after that. He stated that most analysts/economists expected the GDP to be around 3.3% at the end of the year, which suggested that demand/growth was pent up. He stated they were hoping the GDP would be above expectations in the second quarter. He stated that some of the reasons it had been up were bad weather, a strike on the west coast, a general economic slowdown, the complete collapse of commodities prices, and the value of the dollar on a relative basis continued to be better than any other currencies. He noted that wages were starting to move back up, which was something not seen in multiple quarters. He stated that when more people were working and wages were going up, it became inflationary.

Mr. Owens stated that the earnings season was mixed. He stated the decline in Energy prices had an immediate impact on their earnings. He stated the housing market year-over-year was down about 3.0%. He stated the manufacturing and service indices were positive, above 50, which suggested that the economy was expanding. He noted that there had been three years without a significant pullback, and they felt this would continue. He stated they believed there would continue to be slower growth.

Mr. Dupree asked what the next catalyst for a bubble would be, such as in 1999; whereby, Mr. Mulfinger stated that the earnings today were completely different then in 1999, and earnings had continued to rise over that time period.

Mr. Selis asked about the factors that they needed to be wary of; whereby, Mr. Mulfinger stated that some issues were ISIS, the Ukraine in Russia, and Greece's impact on Spain, France and Italy. He stated that in the U.S. we had oil prices, the dollar strengthening, our ability to export and the potential problems to us. He stated that right now there were a bunch of factors that could have a negative impact on us. He stated they saw problems, but they also saw slow growth.

Mr. Selis asked how we could hedge against the factors Mr. Mulfinger just outlined; whereby, Mr. Mulfinger stated that we should try to diversify our assets as much as possible. He stated they expected the economy to grow slowly and interest rates to trend higher, which was bad for bonds. He stated we should diversify the portfolio with the least volatility but at the same time make our investment return.

Mr. Selis asked about the proposed trade agreement and the impact to our funds; whereby Mr. Mulfinger stated that his firm had not made a formal statement as they were still reviewing it and waiting to see what happened.

Mr. Mulfinger stated he favored more diversification in the portfolios and if the portfolios had been in private real estate investing in the past two years, we would have had very good returns relative to the bonds. He stated the market was at an all time high yesterday, and when the market got that way, he wanted to say it was time to reduce the equity allocation, but the only place to put it was into bonds, which he did not think would do well going forward, as it would be hard to meet the investment return assumption by doing so. He stated he favored staying in equity, even though it was more volatile.

Mr. Owens stated that the domestic market was pretty positive across the board, except for the Russell 1000 (Large Cap Value) which was down 0.72% and the broad market (Russell 3000) which was down 0.51%. He stated that smaller companies outperformed larger companies, as the

Russell 2000 Index was up 4.32%, mid-cap index up 3.95% and large cap up 1.59%. He stated they expected that trend to continue if the dollar continued to increase in value. He noted that 50% of the revenue from the S&P 500 companies came from overseas. He stated that if the dollar continued to increase in value, it made their products more expensive to overseas buyers. On a relative basis (companies that did not derive their revenue from overseas), they expected companies that derived their revenue from domestic sources to perform better. He stated that growth outperformed value and smaller outperformed large. He stated that six of the ten sectors of the S&P were positive with Healthcare and Consumer Discretionary being the most positive at 6.5% and 4.8% respectively. He stated that Energy and Utilities were the most negative at -2.90% and -5.20% respectively. He stated the international markets faired very well with the EAFE at 4.88% and local currency at 10.97%. In Emerging Markets, he stated the return was 2.28% with local currency at 4.94%. He stated that the market was a leading indicator which moved before the economy started to move.

In the Fixed Income markets, Mr. Owens stated they were positive across the board. He stated this quarter was the first time in a long time that we had seen some normalcy, as Barclays Capital Aggregate was up 1.61%, Barclays Capital Govt/Credit up 1.60%, Barclays Capital Credit (corporate bonds) up 2.16%, and Barclays Capital High Yield up 2.52%. He stated that interest rates were starting to move up, which would have a negative impact on the value of bonds.

Performance

Mr. Mulfinger stated the value of the General Employees' portfolio was $42,753,000 with a gain net of fees of $337,732. He stated that relative to the benchmark we were below because of HGK, GW Capital, Apex, and Sawgrass's relative underperformance.

Mr. Mulfinger stated that the weightings were overweighted in Large Cap Value, Large Cap Growth, Small/Mid Cap Growth and Small/Mid Cap Value. He stated they were all above the target because the market was going up. He stated the General Employees', Police and Fire plans did not need to balance in Equity, but the Police and Fire plans needed to rebalance back to 30% in Fixed Income. He suggested we should only rebalance to the policy range and not the target, as the target would put a lot of money back in bonds.

Mr. Mulfinger noted that Police and Fire both had cash built up in the Receipts and Disbursements Account (R&D), so the cash could be put into fixed income and then no equity would have to be sold. He stated he did not know what authority Regions had to move money from the R&D account into the managers' accounts. He noted that the Fire plan had an $800,000 buildup of cash, which was too much cash in the fund. He stated he did not know who made the decision to move the cash out.

Mr. Michael Furman asked if they would be rebalancing to March 31; whereby, Mr. Mulfinger stated that they needed to rebalance to what it was the date they rebalanced.

Ms. Towey asked if she should contact Mr. Tim Haugaard, Mr. Mulfinger's associate, for letters of direction; whereby, Mr. Mulfinger stated they could create a spreadsheet with the boards' permission that said where the money should go, but Regions would have to actually move the money.

Ms. Amanda Hayes moved, seconded by Mr. Ken Artin, to approve rebalancing to fixed income to the bottom end of the policy range using available cash on deposit and to give Graystone Consulting the permission to create a spreadsheet for Regions to use to rebalance the fund; and if Graystone Consulting or Regions needed more than the action stated, they would have to come back before the board.The motion passed unanimously.

Mr. Dominic Morgese moved, seconded by Mr. Brian Daley, to approve rebalancing to fixed income to the bottom end of the policy range using available cash on deposit and to give Graystone Consulting the permission to create a spreadsheet for Regions to use to rebalance the fund; and if Graystone Consulting or Regions needed more than the action stated, they would have to come back before the board. The motion passed unanimously.

Ms. Hayes asked if there was a penalty for not rebalancing; whereby, Mr. Mulfinger stated that Mr. Dehner would advise us to stay within the investment policy.

Mr. Dehner stated that the boards could amend the policy, but he advised them to follow the policy at this time.

Ms. Hayes asked if the rebalancing should be done now; whereby, Mr. Mulfinger was recommending it now because he was presenting it. He stated he would make it a policy that when cash was above a certain amount, the money would be moved.

Mr. Artin asked Mr. Mulfinger to ask Regions when money was moved to the managers; whereby, Mr. Mulfinger stated he believed Regions would tell him they did not move it and relied on the city to tell them the amount they needed to keep in the fund to cover the level of expenses.

Ms. McGuire suggested that she, Mr. Mulfinger and Dave Smeltzer of Regions Bank have a conference call to coordinate the rebalancing process.

<u>HGK</u>
Mr. Mulfinger reported that HGK had a -4.29% return vs. the benchmark at -0.72%. He stated this was not a good quarter for HGK and their returns were below the benchmark in all time periods, but in the last five weeks they were up 3.7% vs. 0.93%. He noted that HGK underweighted Healthcare and overweighted Energy, which was the reason for their underperformance.

Mr. Dupree asked Mr. Mulfinger if it was time for a manager search; whereby, Mr. Mulfinger stated that these were annualized returns which meant they looked back at the earnings per year and put all the returns together relative to the benchmark. He stated that this did not say they underperformed every year; and if we broke out the years separately, we would see outperformance and underperformance. He stated that an annualized return did not show year by year returns, but showed the returns over the whole time period. He stated we hired them at the bottom of the market (March 2009), which was not a market cycle. He noted that Mr. Baglio tried to explain the reason they had not outperformed since inception was because they were more defensive, more conservative, and there had only been an up market; therefore, they had not been able to show us how they performed in a down market.

Mr. Furman stated that HGK beat the benchmark in 2011, 2012, and 2013 by a small margin.

<u>Sawgrass</u>
Mr. Mulfinger stated that Sawgrass was more defensive. He reported that for the quarter and one-year time periods, their return was below, but since inception they were above the benchmark. He stated Sawgrass had done better than anticipated at 17.38% vs. 16.91%. He stated we had a higher return, less risk, and they had added value.

<u>Polen Capital</u>
Mr. Mulfinger stated that Polen was more conservative, but concentrated as they had only about 20 securities, which was more volatile. He stated they had a good quarter at 3.72% vs. 3.84%. He reported the one year was above, but since inception they were still below the benchmark. He stated the large cap area had been below overall.

<u>GW Capital</u>

Mr. Mulfinger stated that GW's return was not good at -0.19% vs. 3.02%, as they had overweighted Materials, Energy, Consumer Discretionary and Financials. He stated that the time period we had had them included a down period, and since inception their return was above the benchmark at 17.77% vs. 15.76%.

Apex Capital

Mr. Mulfinger stated that Apex had a bad start at 4.97% vs. the benchmark at 7.44%. He noted the portfolio had the Exchange Traded Funds (ETF) Index for the first nine days of the quarter. He stated that the timing had benefited the portfolio, at 18.83% vs. 21.23%.

Delaware

Mr. Mulfinger stated that the international managers were all above the benchmark for all time periods. He stated that Delaware was overweight in Healthcare and Emerging Markets and underweight in Materials, which benefited the portfolio. He stated Delaware had high return, less risk, and added value.

Renaissance

Mr. Mulfinger stated that Renaissance underweighted Financials and Utilities and overweighted Consumer Discretionary and Telecom, and good stock selection benefited the portfolio. He stated Renaissance had a higher return, less risk and added value.

Garcia Hamilton

Mr. Mulfinger stated that Garcia Hamilton continued to outperform the benchmark in all time periods. He stated they had a higher return with a little less volatility, and had added tremendous value to bonds. He stated their duration was a little longer, which to him was a bit gutsy, but they had been right all along.

Ms. Hayes asked if we were required to keep a certain duration or could the board request a shorter duration; whereby, Mr. Mulfinger suggested the board should not directed Garcia Hamilton as they were hired to make the decision on duration.

Ms. Hayes asked if there was a requirement regarding the duration; whereby, Mr. Mulfinger stated that they were compared to the benchmark, Intermediate Government Credit, and to be around the duration of the benchmark. He stated Garcia Hamilton could make the decision to go a little longer or shorter in duration, and then Mr. Mulfinger evaluated whether their decision was right, and so far they had been right.

Total Return

Mr. Mulfinger stated that the return was below the benchmark at 0.90% vs. 2.21%. He stated the one-year return was below the benchmark at 7.45% vs. 7.93%. He stated the three-year return was above, which very few of their clients were above during that time period. He stated that the five-year and since inception returns were both above the benchmark. Overall, he stated there was higher return and less risk over the whole time period.

<u>Investment Policy Checklist</u>
In the Guidelines, Mr. Mulfinger stated that the General Employees plan had all "Yes's," and Police and Fire had one "No," which the boards had taken care of. Under the Objectives, he stated that the underperformance of HGK, Polen, and Apex had been discussed above.

<u>Risk & Return Analysis</u>
Mr. Mulfinger stated that the returns were a little higher at 6.29% vs. 6.24%, standard deviation at 10.56% vs. 10.95%, beta vs. market at 0.95% vs. 1.00%, market drawdown at -29.47% vs. -31.33%, up capture vs. market at 97.56% vs. 100.00%, down capture vs. market at 95.23% vs. 100.0%. He stated that positive alpha and positive sharp were the reason the portfolio added value and adjusted for risk.

<u>Tactical Asset Allocation (Graystone's view)</u>
Mr. Mulfinger stated that his firm viewed an overweight in the U.S. equity market, an overweight in international markets (Europe and Japan), and underweight in Emerging Markets.

In fixed income, Mr. Mulfinger stated they were underweight in bonds overall, but within bonds, they were overweight in U.S. Investment Grade bonds. We stated we did not hold TIPS, High Yield or Emerging Markets.

Mr. Mulfinger stated they were not allowed to buy REITS, Commodities, Master Limited Partnerships, or Hedge Funds.

8. REPORT FROM FOSTER & FOSTER ON STATE REPORTING OF ADDITIONAL ACTUARIAL DISCLOSURES

Mr. Patrick Donlan, Foster & Foster, distributed the reports for each plan. He stated he would review the General Employees' report with the boards.

Mr. Lee Dehner, Attorney for the Boards, asked if Mr. Donlan had reports for both the state and city to post on their websites; whereby, Mr. Donlan advised that he submitted the report to the state electronically, and this report could be posted to the city's website.

Mr. Dehner asked if this report had the extra 2% calculation; whereby, Mr. Donlan stated that it did.

Mr. Donlan stated that the front page of the report outlined what should be done with the report, as well as a report of the previous five years' assumed and actual rates of return and their respective asset allocations. He stated the Division of Retirement required the information electronically, which he would upload to their website, and the city was responsible for posting the reports to their website.

Mr. Donlan advised that none of the schedules had any impact on the funding requirements of the plans, as the schedules were for statutory compliance purposes only.

<u>GASB 67</u>
Mr. Selis suggested that the first schedule was a worst case scenario; whereby, Mr. Dehner advised that they were designed to make the plans not look well.

Ms. McGuire asked about "Static" and "Generational" in the first two column headings; whereby, Mr. Donlan stated that this was the GASB 67 and 68 information which showed the net pension liability ($8,361,592) that would be required to be listed on the city's balance sheet next year. He noted that "Generational" projected that people would live longer and therefore increase the liability ($9,477,046) to the plan. He further noted that state required a hypothetical liability (worst case scenario) of a return at 5.0% resulting in the unfunded liability increasing to $22,098,258; and then the board favored running it at 9.0% which significantly reduced the unfunded liability to $521,100.

Mr. Mulfinger noted that the longer term return numbers had been over 7.0%.

<u>Asset Sustainability</u>
Mr. Donlan stated that this schedule was a projection of the number of years assets would sustain benefit payments. He noted that this schedule did not take into account the member or city contributions, which was about $2 million this year. He stated that as long as the actuarially determined contribution was made each year, the plan would never become insolvent. He stated that Florida state law also said the plan could not run out of money because the valuation was performed every year and the city had to put in the required contribution.

Ms. McGuire asked what the point of this schedule was, if it was not even a possibility of the funds becoming insolvent; whereby, Mr. Donlan stated its purpose was to make the plans look bad.

Ms. McGuire stated that it had no basis in reality; whereby, Mr. Dehner stated that it was contrary to the requirements of actuarial soundness every year.

Mr. Ken Artin asked about GASB 67 and 68 requirements; whereby, Mr. Donlan stated that GASB 67 and 68 were the best estimate of future experience to develop the liabilities, but the State of Florida was telling us to use a different mortality table and to use 2.0% below the current assumption.

Mr. Artin clarified that this report was not the GASB report and was required by Section 112.664, *F.S.*; whereby, Mr. Donlan stated that was correct. Ms. McGuire commented that the GASB requirements were required to be included in the city's financial report.

Ms. McGuire stated that the annual contribution was based on the calculations by Foster & Foster which included paying down a portion of the unfunded liability.

Mr. Selis suggested that the projected unfunded liability made the city look bad; whereby, Mr. Donlan stated that every city in the country had these pension plans with an associated liability, so we should look at that number relative to other cities to get a better picture.

Mr. Selis asked if raising the target return would give a better sense of what the future unfunded liability would be; whereby, Mr. Donlan stated that the $8 million was the measure of the future benefits compared to the assets of the plan right now. He stated that they had calculated the city's funding requirement to include a payment of $1.2 million which would reduce the unfunded liability.

Mr. Donlan stated that the boards were doing everything they could to keep the funds actuarially sound. He stated the $8 million unfunded liability was not out of the norm. He stated that the funds were becoming better funded through the market returns and extra contributions from the city.

Regarding the assumption, Ms. McGuire stated that it was our managers' responsibility to make the greatest return possible, regardless of the assumed rate of return.

Mr. Selis asked what we could do as a board to direct employees or citizens to the true unfunded liability number; whereby, Mr. Dehner stated that it was important to note that the Division of Retirement would not be publishing the +2.0% number, but it would be included on the city's website. He stated the Division's website would show the 7.0% and 5.0% which would present a negative picture. He stated his recommendation would be to direct them to the city's website which would have the other side of the coin of +2.0% or 9.0%.

Ms. McGuire stated that she could send a note to city employees about the report on the city's website and any questions could be directed to her.

9. DISCUSSION OF SHARE PLAN

Ms. McGuire asked Mr. Donlan about the effect of Senate Bill 172; whereby, Mr. Donlan stated that they would need much more clarification, if it was adopted. He stated that the amount received in 2003 of $223,682 was basically money the city could use as long as the cost of minimum benefits exceeded $223,000, which it would. He stated that amount would be the new guaranteed frozen amount. He stated there was another threshold collected in 2013 of $367,369. He stated that 50% of the excess amounts over $367,369 could be used by the city to offset their funding requirements and the other portion would go into a defined contribution plan for the firefighters.

Mr. Donlan stated that the caveat was that if the city and union agreed on how to use the money, none of the above mattered, but if there was no agreement between the city and union and they obeyed the state methodology, then the city *will* use 50% of the excess to offset their funding requirement.

Mr. Donlan stated that if this law passed, the old frozen amounts were gone. He stated the amount in between $223,682 and $367,369 had to be used for additional benefits over and above the minimum benefits. He stated they would calculate the difference between 2.75% and 3.37% multiplier and if it cost more than $140,000 to provide the benefit, then the city could use all of the $140,000. He stated that there was also a reserve whereby 50% would go to a defined contribution plan for the firefighters and 50% would go to pay down the unfunded accrued actuarial liability (UAAL).

Ms. McGuire clarified that if there was more than $367,369 going forward, the split would be 50% to reduce the city's contribution and on the accumulated money 50% to reduce the UAAL.

Mr. Donlan commented that before this legislation there was a lot of confusion about what happened to the extra money. He noted the original Division's interpretation was that all the extra money would go to provide additional benefits to the firefighters, and then the Naples letter came along and the Division decided the city could have all the extra money. He stated there were a lot of gray areas before this legislation, whereas current legislation says that the money would be split 50/50.

<u>Share Plan</u>
Ms. McGuire clarified that 50% would automatically go into a share plan for the firefighters, so there was no potential for them to increase their multiplier.

Mr. Matt Matheny, Firefighter, asked if the 50% for additional benefits stayed in the plan and earned interest until it was used or did it automatically go into a share plan; whereby, Mr. Donlan stated that the language was very vague about a defined contribution plan and did not say what the benefits were. He stated his vision of it was it would be treated like a share plan.

Mr. Dehner stated that there were some plans that were self-directed, but for the most part the money was invested with the rest of the fund money. He stated that it would be part of the ordinance that designed the share plan.

Mr. Dehner stated that the reason there were not many self-directed plans was because the board would have to take on additional fiduciary responsibility, as a manager search would have to be conducted and it would have to be monitored as part of the fund.

Mr. Matheny asked about the distribution of the share plan; whereby, Mr. Dehner stated that the share plan would have an account value for each person and would be handled similar to the DROP. He stated when the person left employment, they could roll over their share into an ICMA or other similar plan.

Mr. Bozeman stated he favored having his money kept in the fund as our investment managers did a good job of investing the assets of the fund.

Ms. McGuire stated that from a fee perspective she believed we were better off not trying to set up another whole group of managers to manage a very small amount, whose fees would be significant.

10. DISCUSSION OF VESTED MEMBERS ELECTION OF RETIREMENT OPTIONS

Mr. Joe Dupree stated that currently if a member was deceased, his spouse would receive benefits for ten years; but if the member could designate his election selection, the spouse could receive benefits for their lifetime;

whereby, Mr. Dehner stated that the ordinance provided for the death benefit and would have to be amended to add for the lifetime benefit.

Mr. Donlan asked Ms. McGuire about the proposed change to the General Employees' plan; whereby, Ms. McGuire stated that the member was vested at five years, but if the employee was vested but did not have ten years of service, the spouse only received a return on the employee's contribution. She stated that once the employee had ten years of service, the spouse would receive the same benefit as the employee would have gotten at their retirement date.

Mr. Dupree stated that his desire was for 100% to the spouse for life at ten years. He stated he would like to know the cost to the employees; whereby, Mr. Dehner stated that was called a pre-retirement death benefit.

Ms. McGuire clarified that Mr. Dupree was asking that if an employee died prior to retirement that their beneficiary would receive 100% of what they would have gotten at retirement; whereby, Mr. Dehner stated that it would be a pre-retirement death benefit.

Mr. Tommy Bozeman moved, seconded by Mr. Brian Daly, to approve a study by Foster & Foster for a pre-retirement death benefit to the survivor of a vested member at 100% for their lifetime. The motion passed unanimously.

11. DISCUSSION OF FIREFIGHTERS' ORDINANCE AMENDMENT

Ms. McGuire noted that the firefighters were in the middle of collective bargaining negotiations. She asked what would happen if the firefighters approved a contract by June 30 that included a provision for the city to share the $360,000 through a stop/restart of the plan; whereby, Mr. Donlan stated that if the new agreement negotiated the reserve and delineated the annual statement going forward, the law would be moot. Mr. Dehner commented that it would not reach the legislative stream of allocation.

Ms. McGuire clarified that the only way for a portion of the money to be provided to pay down the UAAL was through a stop/restart of the plan. She asked how the stop/restart language would look; whereby, Mr. Dehner stated that it would be two ordinances. Mr. Donlan stated that the state was very strict in that the excess money had to be used for new or additional benefit improvements and a reduction in member contribution rate was a benefit improvement in their eyes.

Mr. Matheny commented that the Division previously did not recognize a contribution reduction as a benefit and then they changed their opinion and now recognize it as an improvement, which would not affect the frozen amount, as a multiplier increase would. He stated that the union felt safe that any stop/restart that only addressed their contribution would not affect the frozen amount.

Mr. Dehner stated that there would be one ordinance to increase the member contribution rate, which would be effective on the immediate adoption of the second ordinance.

Ms. McGuire asked Mr. Dehner if there was another plan that had done this so that she could get language for the contract; whereby, Mr. Dehner stated that they only needed the terms “stop/restart.” Mr. Donlan stated he was looking at an ordinance from Fort Myers recently and their ordinance contained the stop/restart language.

12. ATTORNEY COMMENTS

Legislative Update

Mr. Dehner stated that Senate Bill 172 was presently on the Governor’s desk. He stated that last year the House tacked on some FRS amendments that were not acceptable to the Senate and that was why it was not adopted last year. He stated it was back again this year and had passed by wide margins in the Senate and House. He noted that last year the FLOC and union sponsors of the bill all agreed to it, but this year in the first Senate Committee meeting, the lobbyist for the FLOC, Kraig Conn, appeared before the committee and said the FLOC was opposing the legislation because he said he misread his constituency last year and did not agree with the minimum rate increase to 2.75% and wanted to be able to go to impasse if an agreement was not reached during collective bargaining. He stated that was typically what happened in collective bargaining and usually the employees did not come out well by going to impasse.

Mr. Dehner stated that Senate Bill 172 (former SB 246) and House Bill 341 would affect the police and fire plans providing that the parties would negotiate how the state money would be used and if an agreement was not reached, then it specified a very complicated formula of how the money would be allocated. He stated the Governor may still veto the bill because of the Naples letter which emanated from a letter from the Mayor of Naples to the Governor which led to the Governor and Division of Retirement office changing the interpretation of the use of state money.

Mr. Dehner noted that the Mayor and Governor were next door neighbors and friends, and subsequently there had been a lot of pressure going to the Governor’s office to veto the bill.

Mr. Dehner stated that another bill, Senate Bill 242/House Bill 1309, which was an unfunded state mandate that would impact the pension plans. He stated this bill mandated local law plans such as ours would utilize the same mortality tables and assumptions as FRS and in most cases would increase funding, because the FRS tables projected longer life expectancies than the tables currently being used by local law plans.

Mr. Donlan commented that the next to last page of the report discussed prior showed the "Generational" impact, which was larger on the police and fire and smaller on the general employees, but would increase the funding requirements for all three plans.

Ms. McGuire asked by what authority the legislature had to dictate that to us; whereby, Mr. Dehner stated that the legislature had passed a lot of statutory requirements that the plans had to comply with.

Mr. Donlan stated that the effective date was January 1, 2016, so the funding would not occur until September 30, 2018.

Mr. Tommy Bozeman commented the state was saying pension plans should be *less* of a burden to the cities, but they were enacting legislation that would create *more* of a burden on the cities' pension plans.

Plan Amendments – Tax Compliance

Mr. Dehner stated that he was in the process of amending the plans for tax compliances. He stated it would not have a substantive impact on benefits or funding, but the language was required to be in the plans.

DROP

Mr. Dehner noted that he had received about six favorable termination letters from the IRS regarding the DROP regarding the choice between tying into plan earnings or a stated rate of interest. He stated the IRS took a favorable position.

Mr. Dehner stated Ms. Towey had told him that a police officer had asked if he could leave his DROP money in the plan for 60 days. He advised that the member should be given the special tax notice and suggest he talk to a tax and financial advisor. He stated a lump sum payment out of the DROP was not mandatory and a written request was required to withdraw the money. He stated per the Pension Protection Act of 2006, if a mandatory payment was made and the person was not there to receive it, then an IRA account had to be opened in their name.

Mr. Dehner stated that when DROP participation ceased, all DROP credits also stopped. He stated it was not smart to leave the money in the plan.

<u>Disability Application</u>
Mr. Dehner stated that a disability applicant should maintain employment status until the board had an opportunity to adjudicate entitlement to disability pension, i.e., light duty, leave with pay, leave without pay.

Mr. Dehner stated if an employee resigned, he would not be entitled to the adjudication process because he was not an active plan member any longer. He stated that if the city terminated someone for medical reasons, that was not good either because the board was stopped from finding otherwise.

On the issue of total/permanent disability, Mr. Dehner stated that if the person was terminated for medical reasons, that was an estoppel on the total aspect. He stated there was still the issue of permanent and also the issue of causation whether in-line or not in-line of duty.

Mr. Bozeman asked about the significance of the in-line or not in-line benefit; whereby, Mr. Dehner stated the plan stated the benefit for in-line and not in-line.

Mr. Bozeman asked how an employee would be affected if he was terminated before he applied for disability benefits; whereby, Mr. Dehner stated if he was terminated for medical reasons, estoppel would be the same; and if he was terminated prior to adjudication for reasons other than medical, that would be the end of it. He stated if the person resigned before it was adjudicated, that was the end of it because they would no longer be an active member.

<u>Financial Disclosure</u>
Mr. Dehner reminded the board members to file their financial disclosure forms by July 1.

The General Employees' and Police Officers' Pension Boards adjourned at 11:05 a.m.

Mr. Dominic Morgese left the meeting at 11:07 a.m.

13. OTHER BUSINESS

<u>Ordinance Amendment/AIS</u>
Mr. Joe Dupree asked Mr. Dehner about the ordinance amendment from the contract approved May 20, 2014; whereby, Mr. Dehner stated that Mr. Donlan had prepared the actuarial impact statement (AIS), but he was waiting to see if a couple of other items would be included, such as the share plan. Ms. McGuire advised that the ordinance should be amended according to the provisions in the union contract.

Mr. Dupree stated that he had questions on the April 15, 2015, AIS. He stated there were two employees, one hired before May 20 and on hired after May 20. He stated he felt both employees should have the 3.37% multiplier because the contract had expired; whereby, Mr. Donlan stated that the one hired after May 20 would have a 2.75% multiplier because technically there was no ordinance.

Mr. Dehner stated that he had not started the amendment because of the concessions pending.

Ms. McGuire stated that the ordinance would be retroactive, but one of the firefighters was <u>hired</u> prior to May 20, but became a firefighter after May 20.

Mr. Dehner confirmed that the fire board had seen the April 15 AIS.

<u>DROP</u>

Mr. Dupree stated that the first page of the AIS stated that *"…the projected Normal Retirement Benefits were increased by 0.5%*"; whereby, Mr. Donlan stated that had to do with the way they valued the DROP/Bac DROP, but it did not change any of the benefits.

Mr. Dupree stated that there were three different DROP interest plans (market based, no less than zero and less than zero, and 6.5% guaranteed); whereby, Mr. Donlan stated that the old ordinance said less than zero and the new ordinance would say no less than zero.

Mr. Dupree referred to the Participation under the Deferred Pension Option Plan section and asked about the 35 years of service; whereby, Mr. Donlan stated that this was the maximum period of participation. He stated that the purpose of the DROP was to help the city with turnover issues, so they put a limit of 35 years of service (which included the DROP period).

Mr. Dehner clarified that items one through six listed on page one of the AIS would be the only changes to the ordinance.

<u>Military Buyback</u>

Mr. Dupree stated that some members had expressed interest in buying back prior military service multiple times; whereby, Mr. Dehner stated that the majority of plans allowed multiple requests during the period of employment but it had to be in the ordinance.

Ms. McGuire stated that in their contract it talked about pension improvements and members being able to recommend pension improvements. She stated that the term recommend was somewhat unclear and the city's labor attorney recalled there was some sort of grievance or memorandum of understanding whereby pension enhancements did not have to be negotiated, but they had to go through city staff to get to the City Commission to approve an ordinance amendment. She stated her opinion was that these things were more likely to get in front of the Commission if they went through the bargaining team first.

Mr. Dupree stated that the pension members always have a ton of questions and that was why he had so many things to bring forth at the board meetings. He asked Ms. McGuire if she was the staff that would stop an item; whereby, Ms. McGuire stated that the staff members reviewing items would be herself, the City Manager, Assistant City Manager, and Human Resources Director.

Mr. Bozeman asked if anything that went through the pension board could be stopped by staff before it went to the City Commission; whereby, Ms. McGuire stated that could happen, but these were things that were normally negotiated, as requests for benefit enhancements were generally negotiated first. She stated that the pension board's role was not to circumvent the negotiation process. She stated the pension board's primary role was to manage the assets, not to determine what the benefits were.

Mr. Dupree commented that the website information was outdated, such as the Summary Plan Description dated 2011 and signed by Mr. Michael Marstaller; whereby, Ms. Towey stated that it was the most current SPD and Mr. Marstaller was the chairman at the time.

Ms. McGuire clarified that Mr. Dupree could make as many recommendations as he desired, but that did not mean they would go before the City Commission.

Mr. Dupree stated he felt it was unfair to the board that their recommendation might not reach the Commission; whereby, Ms. McGuire stated that the City Manager had final say regarding what went on the City Commission Agenda.

Mr. Dehner stated that once this ordinance amendment passed, he would prepare a new SPD through that ordinance.

Ms. McGuire stated that staff tried to work with union members before anything went to the board for recommendation.

14. ADJOURNMENT

The meeting was adjourned at 12:05 p.m.

Respectfully submitted,

Lois Towey, Recording Secretary

Attest:

Kelly A. McGuire, Chairman
General Employees' Pension Plan

Ken Artin, Chairman
Police Officers' Pension Trust Fund

Joseph F. Dupree, Chairman
Firefighters' Pension Trust Fund