EMPLOYEES' RETIREMENT SYSTEM OF THE COUNTY OF MILWAUKEE

MINUTES OF THE JUNE 17, 2009 PENSION BOARD MEETING

1. Call to Order

Chairman Dr. Dean Roepke called the meeting to order at 8:34 a.m. in the Green Room of the Marcus Center, 127 East State Street, Milwaukee, Wisconsin 53202.

2. Roll Call

Members Present:
Linda Bedford (Vice Chair)
Donald Cohen
Keith Garland
Mickey Maier
Marilyn Mayr
Jeffrey Mawicke
Dr. Dean Roepke (Chairman)
Guy Stuller

Members Excused:
Dr. Sarah Peck

Others Present:
David Arena, Director of Employee Benefits, Department of Administrative Services
Mark Grady, Principal Assistant Corporation Counsel
Gerald Schroeder, ERS Manager
Gordon Mueller, Fiscal Officer
Dale Yerkes, Assistant to the Fiscal Officer
Vivian Aikin, ERS Administrative Specialist
Sushil Pillai, Milwaukee County Program Manager
Bess Frank, Ad Hoc Oversight Committee
Steven Huff, Reinhart Boerner Van Deuren s.c.
Leigh Riley, Foley & Lardner LLP
Brian Wrubel, Marquette Associates, Inc.
Ray Caprio, Marquette Associates, Inc.
Greg Leonberger, Marquette Associates, Inc.
Marco Ruffini, Buck Consultants
Larry Langer, Buck Consultants
Ben Solnik, Buck Consultants
Terry Chier, Corporation Counsel Intern
Lillie Murphy, Retiree
Gary Knueppel, Husband of Retiree
Steve Schultze, Reporter *Milwaukee Journal Sentinel*

3. Chairman's Report

The Chairman reported that three new travel forms were issued by the Retirement Office. He stated that the Pension Board approves requests for attendance at conferences and travel, not the Retirement Office.

The Chairman noted that Messrs. Cohen and Garland recently attended the International Foundation's conference on portfolio management at the Wharton School.

Dr. Roepke welcomed Ms. Mayr back from her absence.

The Chairman discussed the possible cancellation of the August Pension Board meeting, noting that Mr. Maier would be unable to attend the meeting if it is held. Ms. Mayr stated that traditionally the Pension Board has taken the August meeting off and pointed out that the County Board is on hiatus in August. Several Pension Board members asked Marquette whether there are any decisions that need to be made in August. Mr. Wrubel stated that there is a great deal of work to be done, but the schedule can be rearranged to accommodate the Pension Board's schedule.

The Pension Board unanimously agreed to cancel the August Pension Board meeting unless time sensitive matters arise. Motion by Ms. Mayr, seconded by Mr. Maier.

4. Minutes

(a) Minutes of the May 19, 2009 Special Pension Board Meeting

The Pension Board reviewed the minutes of the May 19, 2009 Special Pension Board meeting.

The Pension Board unanimously approved the minutes of the May 19, 2009 Special Pension Board meeting. Motion by Ms. Bedford, seconded by Mr. Cohen.

In response to a question from the Chairman, Mr. Grady stated that Milwaukee County still has possession of the $30 million from the Mercer settlement. Mr. Grady noted that the topic will be discussed later in the meeting.

(b) Minutes of the May 20, 2009 Pension Board Meeting

The Pension Board reviewed the minutes of the May 20, 2009 Pension Board meeting.

The Pension Board voted 6-0-1, with Ms. Mayr abstaining, to approve the minutes of the May 20, 2009 Pension Board meeting. Motion by Mr. Maier, seconded by Mr. Cohen.

5. Reports of Employee Benefits Director, ERS Manager and Fiscal Officer

(a) Retirements Granted

Mr. Schroeder presented the Retirements Granted Report for May 2009. He reported that 30 retirements were granted in May, noting that 12 retirees elected back DROPs, in amounts totaling $1,013,854.

(b) ERS Monthly Activities Report

Mr. Schroeder indicated that there were 7,333 retirees at the end of May and that ERS paid out $10,173,465 in benefit payments in May.

Mr. Schroeder stated that the percentage of people using direct deposit remains at 96%. He indicated that he will send another batch of letters in July that will encourage the use of direct deposit.

Mr. Schroeder discussed the County's document retention policy. He reported that Retirement Office staff culled through 600,000 documents in the archives over the past 90 days. He commented that 25 years of paper files will be maintained and anything older will be copied to microfiche or DVD. He estimated that it will take at least another year to complete the project.

(c) Waivers – Kelly Reid – Chief Technology Officer, IMSD

Mr. Schroeder reported that four benefits waivers were submitted to the Retirement Office by Ms. Reid, Chief Technology Officer, IMSD.

The Pension Board unanimously agreed to accept the waivers presented by Ms. Reid. Motion by Mr. Maier, seconded by Ms. Mayr.

(d) Cash Flow Report

Mr. Mueller presented ERS's cash flow report and noted that he will be requesting approval for funds for benefit payments for July through September. He reported a correction to the April numbers. Although the report indicates that no funds were disbursed for back DROPs in April, $1,682,310 was disbursed for back DROPs in April and should be reclassified to the lump-sum payments line item from the direct payment – administrative expenses line item.

Mr. Mueller stated that ERS received its request for $5 million for May benefit payments from the pension obligation bond proceeds. He reported that ERS received the County's final 2008 contribution of $3.3 million. He indicated that ERS will need $10 million per month for July, August and September for benefit payments. In response to a question from the Chairman, Mr. Mueller stated that ERS maintains a two month cash reserve in anticipation of a situation where benefit payments exceed the amount he requested at the Pension Board meeting. Mr. Mueller commented that income and expenses do not come in ratably, which makes it hard to predict ERS's monthly cash needs.

In response to a question from Ms. Mayr, Mr. Mueller stated that ERS will have lower administrative expense cross charges, but pointed out that some expenses will be higher, such as salaries due to the increase in Retirement Office staff. In response to a question from Ms. Bedford, Mr. Mueller stated that after the Pension Board approves the funds request, he will ask Marquette to decide the source of the funds, which has recently been taken from uninvested funds in the cash overlay account.

The Pension Board unanimously approved the Fiscal Officer's request of $10 million per month for July, August and September for benefit payments from a source to be determined by Marquette. Motion by Ms. Mayr, seconded by Mr. Cohen.

6. Investments

(a) Marquette Associates, Inc. Report

Mr. Wrubel introduced Mr. Leonberger as part of the Marquette team, noting that Mr. Leonberger assisted with the asset allocation study. Mr. Caprio reviewed the ERS portfolio's asset allocation. He reported that ERS has approximately 50% of its assets invested in fixed income. He commented that fixed income investments were as volatile as equities in May. He noted that there has been a bear market rally. He commented that large cap space outperformed small and mid cap spaces. Mr. Wrubel pointed out that the 10 year average return in the overall market has been 6% in the bond market and -2% for the equity market. He stated that the asset allocation and investment decisions made by the Pension Board and its investment managers have a big impact on the portfolio's performance. He explained that ERS has a long-term liability with its future pension benefit payments, so ERS must look at long-term returns when developing its asset allocation.

Mr. Caprio reported that 2009 has been a favorable year for emerging markets, which are smaller countries with lower GDP. He commented that emerging markets also provide good currency exposure and diversification. He stated that

ERS has exposure to emerging markets and some managers have access to emerging markets. He indicated that ERS has no exposure to hedge funds. He noted that there are two types of hedge funds, true hedge funds and long/short hedge fund of funds. He explained the difference between the two types and pointed out that traditional equity managers utilize long only investment strategies. He opined that hedge funds provide good diversification to a portfolio and help create more market-neutral portfolios.

Mr. Caprio provided a status update on Pension Board action items. He reported that ERS initiated requests for proposals ("RFPs") for small cap and emerging markets investment managers.

Mr. Caprio stated that Bank of New York Mellon came to ERS with options regarding the reinvestment of cash in Bank of New York Mellon's securities lending program. He indicated that the two choices were to remain in the lending program or to reinvest the cash into a separate account, and that the separate account option was selected.

Mr. Caprio reported that ERS assets were valued at $1.538 billion as of April 30, 2009, which includes the pension obligation bond funds. He indicated that ERS is not in line with its target asset allocations, but is getting closer to its targets with the market rebound. He stated that Marquette does not recommend a rebalance until after the asset allocation study is completed.

Mr. Wrubel stated that ERS's assets increased in value by 4.4% in April and that the May performance figure will also be positive. Mr. Caprio stated that ERS has positive performance for 2009 year-to-date. He reviewed ERS's investment managers' performance through April. He commented that one goal of the asset allocation study is to reduce volatility in the portfolio. He stated that ERS may want to consider diversifying its small cap space by adding a fundamental manager to complement AQR. He indicated that Westfield is below its benchmark and that the Capital Guardian portfolio was liquidated into the GMO portfolio effective June 2, 2009.

Mr. Caprio reviewed the new reporting format for ERS's private equity investments. He noted that Marquette has broken down all ERS private equity investments by inception, amounts committed, called and distributed, fees and the value of the investment. He indicated that ERS has an 8.17% net annualized IRR since inception on its private equity investments.

The Chairman stated that he attended Adams Street Partner's annual conference on June 4, 2009. In response to a question from the Chairman, Mr. Wrubel explained that Adams Street Partners is using secondary market investments to try and attempt to reduce volatility by purchasing interests in existing investments, with the hope that the existing interest will increase in value. Mr. Wrubel explained that the secondary market is one way to liquidate private equity investments.

In response to a question from Mr. Garland, Mr. Wrubel explained the reasons for Adams Street Partner's negative performance figures. Mr. Wrubel stated that Marquette is expecting lower returns for Adams Street Partners, but Marquette is hopeful that the returns will not remain negative. In response to a follow up question from Mr. Garland, Mr. Wrubel indicated that Marquette expects positive performance for Adams Street Partners over the next 5 to 7 years with an IRR between 5%-10%.

In response to a question from Mr. Garland, Mr. Wrubel explained that Adams Street Partners is a fund of funds. Mr. Wrubel stated that Adams Street Partners is one of the top four fund of fund managers in the world and invests in 30 to 50 funds, which exposes ERS to hundreds of companies. He commented that Adams Street Partners is extremely diversified and that he could provide the Pension Board with a list of Adams Street Partners' investments, if desired. The Chairman stated that he could provide any interested Pension Board members with the conference materials.

Mr. Caprio reviewed the fees ERS pays to its investment managers. He stated that Marquette has been able to renegotiate fees with several managers. He reported that ERS pays 21 basis points in manager fees, which is less than the average fees paid.

Mr. Wrubel discussed how the asset allocation study will be a key driver of the future of the ERS portfolio. He stated that ERS generally has a high quality portfolio. He noted that it was good that ERS did not have much equity-type real estate in its portfolio because the sector was beaten up and was difficult to liquidate. He indicated that equity-type real estate is an attractive investment now because investors can purchase these investments at depressed prices.

Mr. Leonberger explained how Marquette used a Monte Carlo model to simulate economic trends to produce the asset allocation study. He stated that Marquette took 1,000 different scenarios and determined the effects those scenarios would have on the various asset classes under consideration during the asset allocation study.

Mr. Wrubel reviewed ERS's cash flow situation. He pointed out that there is a large mismatch between contributions and benefit payments, which causes deficit spending. He noted that ERS needs to earn its 8% target rate of return (net of fees). He discussed ERS's historical funding ratio. He indicated that ERS was 108% funded in 2002. He noted that the annual funding ratio has declined despite the market turnaround between 2003 and 2006.

Mr. Wrubel explained the portfolio options, which contained all potential asset classes and their relevant benchmarks. He discussed the composition of the current portfolio and the benchmarks used in modeling. He stated that Marquette developed many model portfolios but only presented the best options in its report to the Board. He indicated that Marquette was directing the Pension Board towards Portfolio D. He noted that the Investment Committee discussed the portfolio options at the Investment Committee meetings.

Mr. Wrubel stated that the current portfolio is too reliant on the performance of the stock market. He reported that ERS has 52% exposure to equities and 7% to high-yield fixed income, which performs similar to equities, and a percentage to REITs, which gives ERS over a 60% exposure to equities or equity-like investments. He indicated that ERS will perform well when the market rallies, but in a poor market, ERS will not achieve its 8% target rate of return. He commented that ERS should focus on avoiding portfolio risk. He pointed out that ERS's large exposure to equities presents risk, and the Pension Board should consider shifting the portfolio's asset allocation away from equities.

Mr. Wrubel compared the current portfolio to Portfolio D. He indicated that ERS currently has 42% allocated to bonds. He suggested reducing the percentage allocated to BarCap Aggregate asset class from 35% in the current portfolio to 32%, and reducing the percentage allocated to the BarCap High Yield asset class from 7% to 0%. He noted that ERS would be redistributing the high risk bond portfolio to less volatile asset classes to reduce risk by doing so. He stated that ERS would reduce is current allocation to cash of 1% to 0%.

Mr. Wrubel stated that the overall trend is to reduce ERS's exposure to equities. He reported that ERS would reduce its allocation to the S&P 500 asset class from 7% to 6% and its allocation to the Russell 1000 Value asset class from 8% to 7% by adopting Portfolio D. He indicated that Portfolio D would reduce ERS's exposure to the Russell 1000 Growth asset class to zero from 5% because this asset class is difficult to outperform on a regular basis. He also noted that ERS would reduce its allocation to the Russell Midcap Value asset class from 3% to 0%, and increase its allocation to the Russell Midcap Growth asset class from 3% to 5%. He explained that Portfolio D would increase the allocation to Russell 2000 Value asset class from 2.5% to 5%, while decreasing the allocation to the Russell 2000 Growth asset class from 2.5% to 0%.

Mr. Wrubel pointed out that Portfolio D would allocate 7% to equity-type real estate from the current 3% allocated to REITs. He commented that Portfolio D would allocate 7% to infrastructure and 10% to hedge fund of funds, both of which would be new asset classes for ERS. He stated that the international allocation would remain relatively the same, but would be redistributed more towards emerging markets. He stated that the allocation to the MSCI EAFE asset class would decrease from 16% to 12%, the allocation to the International small cap asset class would decrease from 4% to 3%, while the allocation to the MSCI Emerging market asset class would increase from 0% to 3%.

In response to a question from Mr. Garland, Mr. Wrubel stated that the 8% target rate of return is closer to 8.5% after factoring in fees and costs.

Mr. Wrubel explained that the current portfolio has a 59% chance of not achieving an 8% rate of return, while Portfolio D has a 28.5% chance of not achieving an 8% rate of return. Mr. Leonberger stated that ERS wants to achieve a higher rate of return with lower volatility and downside risk. In response to a question from Mr. Grady, Mr. Wrubel and Mr. Leonberger stated that adding more hedge funds, private equity and infrastructure to the portfolio would create more illiquidity because it is difficult to come up with cash from alternative investments in difficult times like now.

In response to a question from Ms. Bedford, Mr. Wrubel stated that the current market shows that hedge fund of funds perform better than fixed income investments, so ERS will probably see an immediate impact on the portfolio as a result of investing in a hedge fund of funds. He indicated that it will take approximately 2 to 5 years for the real estate investments to have an impact on ERS, while infrastructure investments will take between 5 to 10 years to have an impact, but will include income generating investments. He noted that it will take several years to see the long-term impact of these investments on ERS.

In response to a question from Mr. Grady, Mr. Caprio stated that ERS will need to revise its investment policy benchmarks over a period of time as ERS moves towards its portfolio goals. In response to a follow up question from Mr. Grady, Mr. Caprio stated that ERS should still be in line with its peers after adopting Portfolio D. Mr. Wrubel pointed out that many pension funds have actuarial rates of return different than 8%. He noted that plans with greater than $1 billion in assets are more similar to ERS, as these plans typically have negative cash flow rates and 8% actuarial rates of return.

Mr. Wrubel explained that if ERS is in the top 40% of its peers consistently, it will be in the top quartile of performers over a 4 to 7 year period. Mr. Grady stated that ERS has done well in the past due to its over-weighting to fixed income and he assumes that infrastructure and hedge funds will provide the same minimal volatility effect. Mr. Wrubel stated that interest rates have come down in the past 20 years and the right time to reallocate fixed income is when interest rates start going up, as they are now.

In response to Ms. Riley's question, Mr. Caprio stated that Marquette's quarterly report measures ERS's performance attribution by asset allocation and manager selection. In response to a question from Mr. Garland, Mr. Wrubel explained how hedge funds function. He stated that an investor is hedging equity in a fund of funds. The fund of funds manager will invest in hedge funds that invest in a combination of long and short equity strategies in domestic or foreign equities. He commented that these fund of funds reduce the risk of equities in the portfolio and are transparent, which makes them easy to value. He noted that funds of funds are usually not leveraged, and are not multistrategy funds that also invest in fixed income, which makes an investment difficult to price.

In response to a question, Mr. Wrubel discussed why hedge fund of funds are not like Madoff-type funds. He stated that the underlying investments are a transparent equity class, the investments are priced by an outside third party source and they utilize custodians and broker dealers other than the investment manager.

Mr. Wrubel stated that Marquette formally recommends that the Pension Board adopt Portfolio D as its target asset allocation.

In response to a question from Mr. Maier, Mr. Wrubel stated that there really are only 600 to 700 hedge fund managers who are appropriate for the institutional grade investor. He noted that there are only 10 large fund of fund managers. He commented that a good fund of funds manager needs both operational and investment side employees. Mr. Maier inquired whether the difference between Portfolio C and D was due to the difference in valuation methods. Mr. Wrubel stated that investments' values are now marked to market. He indicated that real estate investments are usually valued annually by appraisers. He noted that infrastructure is more difficult to value and is valued by taking the discounted cash flow of the infrastructure.

In response to a question from Ms. Riley, Mr. Leonberger stated that Portfolio D is concentrating mid cap value and small cap growth from two asset classes each into one because Marquette expects better performance based on internal research. Mr. Wrubel commented that it is more optimal to focus on growing companies.

In response to a question from Mr. Stuller, Mr. Wrubel indicated that the Investment Committee discussed the effects of the switch to Portfolio D on the current investment managers. He noted that Westfield, Boston Partners, Loomis Sayles (high-yield) and Mellon Capital Management will all be impacted by the switch to Portfolio D. In response to a follow up question from Mr. Stuller, Mr. Maier stated that the Pension Board will discuss the asset allocation switch with the managers when they come to the Pension Board meeting.

In response to a question from Mr. Garland, Mr. Grady explained that an extensive RFP process has been initiated for investment managers for new asset classes. In response to a question from Ms. Mayr, Mr. Wrubel stated that there will be approximately a two-year schedule to fully implement Portfolio D. In response to a question from the Chairman, Mr. Caprio stated that the Pension Board will need to extend the asset allocation ranges to stay in compliance with its investment policy while implementing Portfolio D.

Mr. Maier provided a report on the Investment Committee's discussion of the asset allocation study. He indicated that Portfolio D is an attractive option because it appears to reduce risk while bringing the average return closer to 8%. He noted the Investment Committee approved investment manager searches in the Portfolio D context. He stated that the Investment Committee has much to learn about the new asset classes, especially with the infrastructure asset class. He commented that the asset allocation study is headed in a good direction and the Investment Committee will continue in that direction, but the Investment Committee still has homework to do.

Mr. Maier stated that the Pension Board will need to work towards implementing Portfolio D and develop a transition plan. Ms. Riley answered Ms. Mayr's question regarding adjusting the target percentages to stay in compliance with the asset allocation policy.

Mr. Garland commented that he wants to have action items on the agenda before he is asked to vote on them. Mr. Grady stated that the goal is to work towards implementing Portfolio D by having the Pension Board members educate themselves on the new asset classes, hire managers for those asset classes and to then fund the investments.

Mr. Mawicke explained that the Pension Board would be choosing Portfolio D as a way to take steps toward decreasing volatility in the portfolio, minimizing risk and increasing return. He pointed out that the 1990's investment philosophy of "everything will go up" are over. He pointed out that Portfolio D gives ERS the best chance to achieve its desired goals and target rate of return.

The Pension Board voted 3-5, with Messrs. Mawicke, Maier, Cohen, Dr. Roepke and Ms. Bedford dissenting, to hold over the adoption of Portfolio D until the July Pension Board meeting. Motion by Mr. Garland, seconded by Ms. Mayr.

Ms. Mayr stated that she wants to receive more information on certain aspects of Portfolio D before adopting Portfolio D. Mr. Wrubel stated that Marquette has worked with infrastructure and hedged equities often and believe that the Pension Board can get comfortable with these asset classes. Ms. Bedford noted that the Investment Committee has studied the asset allocation issue for 6 months and is comfortable with Portfolio D. She commented that the Investment Committee would not bring the recommendation to the Pension Board if it were not satisfied that Portfolio D is the Pension Board's best option.

The Pension Board voted 5-3, with Messrs. Stuller and Garland and Ms. Mayr dissenting, to implement Portfolio D as formally recommended by Marquette with the proposed allocations to long/short strategies and infrastructure not to be implemented until the Pension Board has received more information on these asset classes and specifically voted on implementation and manager or investment fund selection. Motion by Mr. Cohen, seconded by Mr. Maier.

Mr. Grady advised that the Pension Board should consider whether it should respect the committee structure or develop an alternative. Mr. Garland suggested presenting the action items before the meeting. Ms. Mayr stated that each member has a fiduciary duty to be fully informed before making a decision.

A Marquette representative recommended approving a transfer of $66 million of pension obligation bond funds that are currently being overlayed to three investment managers: $35 Million to Baring Asset Management, $18 Million to GMO large cap and $13 Million to GMO small cap.

The Pension Board unanimously approved Marquette's recommendation to transfer $66 million in overlayed pension obligation bond funds to Baring Asset Management and GMO as outlined in its formal recommendation. Motion by Mr. Maier, seconded by Mr. Mawicke.

Mr. Caprio discussed the RFP for transition managers. He explained that the purpose of a transition manager is to move money between investment managers at the lowest cost and to reduce market exposure. He stated that transition managers typically act as fiduciaries and are used by a majority of public funds. He indicated that Marquette sent out the RFP to the 12 transition managers it works with the most.

Mr. Wrubel reviewed the requirements listed in the RFP, which included whether the transition manager will agree to act as a fiduciary, its experience and proposed fee. He stated that Marquette wants high quality transition managers to choose from to best transition the asset class that is being transitioned. He reported that the Investment Committee chose four transitional managers: JPMorgan, Black Rock, State Street Global Advisors and Global Transition Solutions. He pointed out that Black Rock provided the lowest domestic fee and has good exposure to all ERS asset classes. He indicated that these four would serve as a bullpen of managers and each individual transition will be bid out to the four managers, after which the best manager for that task would be selected.

Mr. Wrubel stated that all four managers provide pre and post transition reports. In response to Mr. Garland's question, Mr. Wrubel stated that Marquette has had satisfactory interactions with all four transition managers in the past. In response to a question from Ms. Mayr, Mr. Caprio responded that the cost varies for each transaction based on size and asset class.

In response to a question from Ms. Mayr, Mr. Caprio stated that each contract will be for three years. Mr. Grady clarified that each manager knows they may not be awarded any work, that ERS can terminate each contract at any time and the Pension Board could issue RFPs for additional transition managers.

The Pension Board unanimously agreed to accept the recommendation of the Investment Committee to enter into contracts with JPMorgan, Black Rock, State Street Global Advisors and Global Transition Solutions for transition management services and to bid out the transitions to the four managers through Marquette as they occur. Motion by Mr. Cohen, seconded by Mr. Maier.

(b) Investment Committee Report

Dr. Roepke reported that the Pension Board discussed all of the Investment Committee's recommendations made at its last meeting during Marquette's presentation.

7. Audit Committee Report

Mr. Stuller, the Chair of the Audit Committee, reported on the June 5, 2009 Audit Committee meeting. He indicated that the Audit Committee set its future meeting dates and discussed and accepted a formal Audit Committee charter. He reported that the ERS Fiscal Officer will discuss the auditor's findings and the audit report at the July Audit Committee meeting and the auditor will present at the July Pension Board meeting. He stated that the Audit Committee continues to analyze Rules 1013 and 1043 with respect to benefit options and survivorship benefits. He noted that the Audit Committee agreed that the Retirement Office should ask disability pensioners to provide their income tax returns at the time of disability retirement in addition to disclosing any secondary income they earned prior to becoming disabled.

8. Actuarial Valuation Report and County Contribution Request

Mr. Langer introduced the members of the Buck actuarial team assigned to ERS and presented the actuarial reports for ERS and OBRA as of January 1, 2009 to the Board. Mr. Langer invited the Pension Board members to ask questions during the presentation. He provided an overview of the 2008 plan year. He stated that the actuarial rate of return for 2008 was 3.4%, while the market rate of return was -22.5%. He noted that the ERS assets are smoothed and averaged over a period of time. He commented that the actuarial rate of return was below the 8.0% target rate.

Mr. Grady pointed out that OBRA assets are not smoothed. Mr. Langer stated that ERS and OBRA's liabilities have behaved as planned. He noted that Buck assumed that the proposed Ordinances regarding actuarial assumptions and treatment of certain items are going to be adopted. He commented that 2008 was a very difficult year and that the County will need to increase its contributions to ERS in future years. He noted that the proceeds of the pension obligation bond sale are reflected in the valuation and are being used to offset existing contribution shortfalls, with the remainder to be amortized over 30 years. Mr. Langer explained that if the remainder were to be amortized over five years as required under the contribution variance provisions of the Ordinance, no contributions would be made over the next 6 ½ years. If the County Board made no contributions for 6 1/2 years because of the pension obligation bonds, the funded status would drop to 55%. He noted that by phasing the pension obligation bonds in over 30 years, it will increase the required contribution amounts in the short term compared to the contributions required under the current Ordinance provisions.

Mr. Langer stated that the County Board Ordinance relating to the pension obligation bonds creates a fresh start on contribution variances by covering shortfalls. ERS received $397 million from the pension obligation bonds of which $33 million will be used immediately to cover unamortized prior contribution variances, with the remainder being amortized over 30 years.

In response to a question from Mr. Stuller, Mr. Langer stated that the Pension Obligation Bond Working Group, comprised of County employees, the actuary, and investment advisors, developed this plan. Mr. Langer stated that Milwaukee County must pay off the pension obligation bonds over 25 years, which results in $35 million per year in payments for debt service and the stabilization fund. In response to a question from Mr. Stuller, Mr. Grady stated that the Pension Board must comply with the proposed Ordinance, if enacted, which would require greater County contributions to ERS over the next 6 years than there would be without the change to the County Ordinances to implement pension obligation bonds.

Mr. Garland asked whether an 8% target rate of return is too high. Mr. Langer stated that Buck looks at the rate of return every year and performs an in-depth review every five years. He indicated that the Pension Board must take a long-term view of the target rate because investment returns have very long time horizons. He indicated that the actuary and the investment consultant review the 8% target, and that there is no need to reduce the target rate if the Pension Board believes it can obtain the 8% rate of return over the long-term. Mr. Grady pointed out that one of the reasons for the change in asset allocation is that the current portfolio has a 60% chance of not hitting the 8% target.

Mr. Langer indicated that most retirement plans follow the same annual review and update process as ERS. Mr. Ruffini reviewed the actuarial model for projection of future benefits which determines the contribution amount. He stated that the actuary needs membership data, benefit provisions, asset data, actuarial assumptions and the funding methodology in order to determine the unfunded accrued liability, funded status and employer contribution. He explained that the unfunded accrued liability is the amount of benefits earned to date for which the plan does not have cash on hand to pay those benefits when they are projected to come due.

Mr. Ruffini reviewed ERS's actuarial assumptions. He commented that Buck and the Pension Board review the actuarial assumptions on an annual basis to determine if they reflect reality. He stated that Buck performs a more detailed analysis that compares the actual historical experience to the actuarial assumptions every five years to determine whether the actuarial assumptions should be revised. He indicated that the next actuarial study is scheduled for 2012.

Mr. Langer described the cost method actuarial valuation process. He explained that under the cost method, the actuary determines what future benefit payments will be by determining how much service credit a member has and how much he or she will have. He stated that this normal aggregate entry age cost method is the most common method used for public plans.

Ms. Mayr questioned whether Buck has a conflict of interest in reporting to the County Board and the Pension Board. Mr. Langer stated that Buck must be comfortable providing this actuarial advice to either body and the advice helps ERS.

Mr. Langer said that public plans express their benefits costs as a percentage of payroll and ERS's payroll grows at 3.5%

Mr. Langer stated that ERS is a stable and mature fund as demonstrated by the number of active, retired and deferred vested members. He discussed a chart showing the market and actuarial values of ERS's assets for the past 10 years. He commented that the graph is skewed in 2009 due to the pension obligation bonds receivable and the 2008 investment losses.

Mr. Langer explained the ERS market value reconciliation. He stated that the actual loss in 2008 was approximately $486 million and will be spread out over 5 years. He indicated that the estimated rate of return in 2008 was -22.5%. He explained how Buck calculated the actuarial value of ERS's assets. He noted that ERS phases in gains and losses over 5 years.

Mr. Langer reviewed the unfunded accrued liability of ERS for 2008 on an actuarial value basis. He indicated the level of assets that ERS should have if it were 100% funded. He stated that if ERS were 100% funded the County would only need to contribute the amount of benefit payments accrued during the year, which would have been $21 million.

He reported that ERS and OBRA's actuarial funded status is 95.5%, while the actual market value funded status is 77.4%. He pointed out that the 95.5% actuarial funded status is projected to decrease to 77.4% over the next 5 years as deferred losses are amortized and contributions will go up over the next few years.

Mr. Langer commented that the receipt of the pension obligation bonds proceeds reduced the 2009 actual contribution. He reconciled the 2009 budgeted contribution to the 2009 actual contribution. He explained the reconciliation of the actual 2009 contribution to the 2010 budgeted contribution, noting that the $8 million increase in contribution was attributable to the phase in of deferred losses.

In response to a question from Ms. Mayr, Mr. Ruffini stated that the $30 million Mercer recovery was not included in the valuation because it was not in process as of January 1, 2009 unlike the pension obligation bonds. Mr. Grady indicated that there is a resolution, but no Ordinance regarding the treatment of the $30 million.

The Pension Board voted 7-1, with Mr. Stuller dissenting, to approve the $31,017,000 2009 actual County contribution to ERS and the $39,335,000 2010 budgeted County contribution to ERS, contingent upon passage of the County Ordinance by the County Board to implement the pension obligation bonds. Motion by Mr. Garland, seconded by Mr. Cohen.

9. <u>35 Hour Work Week for Retirement Office Employees</u>

At the request of the Chairman, Mr. Arena stated that the 35 hour work week would take effect June 28 through the end of the year.. The Chairman reported that he wrote a letter to the County Executive requesting an exemption for the Retirement Office from the mandated 35 hour work week. The Chairman indicated that he wrote that the Retirement Office has traditionally been understaffed and is currently addressing important compliance issues. He also wrote that ERS pays the Retirement Office salaries and exempting ERS from the 35 hour work week would have no impact on County costs or the budget. The Chairman noted that he has not received a response.

Mr. Pillai stated that the Vitech project is at a critical juncture and the 35 hour work week would have an adverse effect on the project. He indicated that Releases 2 and 3 and the fixes to Release 1 are extremely critical to the success of the project. He noted that he wants the consultants to be finished by the end of 2009 and make the knowledge transfer to County employees. He calculated that the shortened work week would cost the Retirement Office approximately 2,600 of lost labor, or about the equivalent of losing two full time employees. In response to a question from Mr. Stuller, Mr. Pillai stated that 20 Retirement Office employees work on the Vitech project.

Ms. Mayr questioned whether Mr. Grady or Corporation Counsel needs to go to the County Executive because the Pension Board is not the party shortening the work week and the Pension Board has no control. Mr. Grady stated that the Pension Board could make a request as part of a motion requesting that the Retirement Office staff be exempted. In response to a question from Ms. Mayr, Mr. Arena stated that he has not requested an exemption.

The Pension Board voted 7-1, with Mr. Stuller dissenting, to authorize and direct the Chairman to send a letter to the County Executive requesting an exemption from the 35 hour work week for Retirement Office staff. Motion by Mr. Garland, seconded by Ms. Mayr.

Mr. Grady said there will be no effect on retirement credit as the result of the 35 hour work week.

10. Administrative Matters

Mr. Cohen stated that he and Mr. Garland attended the International Foundation's program on portfolio construction at the Wharton School. Mr. Cohen commented that the program was very beneficial and included outstanding presenters. Mr. Garland noted that attendees were able to evaluate other municipalities' investment programs. Mr. Cohen expressed interest in attending the follow up course in September.

The Pension Board unanimously approved the attendance of any interested member at the International Foundation's program on portfolio construction in September 2009 at the Wharton School. Motion by Ms. Bedford, seconded by Mr. Maier.

The Pension Board had no additions to or deletion from the future topics list.

11. Disability Pensions – Colleen Babich – Excess Earnings

Ms. Bedford moved that the Pension Board adjourn into closed session under the provisions of Wisconsin Statutes section 19.85(1)(f) with regard to items 11, 12 and 13 for considering the financial, medical, social or personal histories of specific persons which, if discussed in public, would be likely to have a substantial adverse effect upon the reputation of any person referred to in such histories and under section 19.85(1)(g), with regard to items 11, 12 and 13 for the purpose of the Board receiving oral or written advice from legal counsel concerning strategy to be adopted with respect to pending or possible litigation. At the conclusion of the closed session, the Board may reconvene in open session to take whatever actions it may deem necessary concerning these matters.

The Pension Board voted by roll call vote 7-1, with Ms. Mayr dissenting, to enter into closed session to discuss agenda items 11, 12 and 13. Motion by Ms. Bedford, seconded by Mr. Cohen.

The Pension Board discussed Ms. Babich's situation in closed session.

Upon returning to open session, the Pension Board approved Corporation Counsel's settlement with Ms. Babich regarding the repayment of her excess disability pension, subject to approval by the Internal Revenue Service as part of the closing agreement for ERS's VCP application. Motion by Mr. Mawicke, seconded by Mr. Maier.

12. Valerie Knueppel Claim Appeal – Retroactive Pension Adjustment

Mr. Knueppel presented his wife's appeal regarding a retroactive pension adjustment to Ms. Knueppel's pension benefit. He indicated that he believes she is being penalized because she retired on February 4, 2008, her 55th birthday, but did not begin receiving her pension until March 1, while a person who retires effective February 28, 2009 receives his or her pension March 1. Mr. Knueppel read from a letter that contained the facts of his wife's appeal and discussed hypothetical scenarios in which he believes members are not receiving up to one month of benefits.

The Pension Board discussed Ms. Knueppel's appeal in closed session.

Upon returning to open session, the Pension Board unanimously agreed to refer Ms. Knueppel's appeal to Corporation Counsel for evaluation and to lay over her appeal until a future meeting for further discussion. Motion by Mr. Cohen, seconded by Mr. Stuller.

13. Lillie Murphy Claim Appeal – Retroactive Pension Adjustment

Ms. Murphy presented her appeal for a retroactive pension adjustment. She stated that in November 2008, the Pension Board denied her pension because it held she was terminated for cause, which made her ineligible for a pension under ERS Rules.

Ms. Murphy stated that she appealed the Pension Board's decision and the Pension Board reversed its original decision in light of new facts at its March 18, 2009 meeting. Ms. Murphy indicated that she received a letter on April 14 stating she was retired effective January 1, 2009. She reported that her benefits began in May but she did not receive any benefits for January, February, March and April. She requested payment for those months.

The Pension Board discussed Ms. Murphy's appeal in closed session.

Upon returning to open session, the Pension Board voted 5-2, with Mr. Mawicke and Ms. Mayr dissenting, to approve retroactive payment of pension benefits to Ms. Murphy for January through April 2009. Motion by Mr. Maier, seconded by Mr. Cohen.

14. Pending Litigation

Mark Ryan, et al. v. Pension Bd.

The Pension Board determined that there is nothing new to report on in the above captioned litigation.

15. Report on Special Investigation

The Pension Board determined that there is nothing new to report regarding the special investigation.

16. Report on Compliance Review

The Pension Board determined that there is nothing new to report regarding the compliance review.

17. Adjournment

The meeting adjourned at 2:45 p.m.

Submitted by Steven D. Huff,
Secretary of the Pension Board