

August 10, 2010
Minutes #462

Minutes of the Board of Trustees' Meeting -1-

- Call to Order:** Chairman, Donald Pinard called the meeting to order at 8:30 a.m.
- Present:** Trustees: Chairman, Donald Pinard, Jennie Angell, Richard Molan, Paul Porter, Chuck Hungler and Bill Sanders arrived at 8:32 a.m.
MECRS Staff: Gerard Fleury, Sandi Aboshar and Suzanne Wilson
- Absent:** Trustees: Mayor Ted Gatsas
- In Attendance:** Attorney John Rich of the McLane Law Firm
Mr. Kevin Leonard and Sebastian Grzejka of New England Pension Consultants

Approval of the Minutes of the Previous Board Meeting:

A motion was made by Trustee Angell to approve the minutes of the July 13, 2010 board meeting, seconded by Trustee Hungler and passed unanimously by all those trustees present.

Approval of the Immediate Meeting Agenda:

Trustee Angell made a motion to accept the immediate meeting agenda, seconded by Trustee Porter and passed unanimously by all those trustees present.

Report of the Executive Director:

Monthly Status Report on Pension Administration System Upgrade/Replacement – Mr. Fleury reported the analysis has continued on the Pension Administration System Upgrade. Further vendor inquiries requested by the MECRS Administration & Accounting Committee in July were made, replies have been received, and the information is being summarized. Responses from all vendor references have also been received and two Massachusetts Public Plans have been selected for site visits at the end of the month, to review their pension applications in operation.

Monitoring of GASB Pronouncement – Next, Mr. Fleury noted that changes in the reporting requirements in the MD&A, (Management Discussion & Analysis) section of the CAFR, (Comprehensive Annual Financial Report) may become effective for the 2010 reporting period. Also he noted that since the composition of the MD&A is the responsibility of the reporting entity, MECRS will need to understand how the new requirements impact public plans and amend its reporting format accordingly. On July 28th, the Segal consulting firm conducted a web seminar on the

Minutes of the Board of Trustees' Meeting -2-

likely impact of GASB changes and MECRS was allowed to participate at no charge. Mr. Fleury reported first that GASB may not implement all of the new requirements in their existing form. However, one key element of the proposed changes in the requirement that fluctuations in the market value of investment assets in excess of 15% be recognized in the same period. Should that be enacted, Mr. Fleury commented that it may result in volatility in the reported employer funded ratio unlike anything previously seen in public plans. Although the funded ratio may see increased volatility as a result of the proposed rule, it will not result in increased employer contribution volatility. The reason for this is the proposed rules also decouple the funded ratio from employer funding obligations in order to avoid wild swings in the employer contribution rates. Mr. Fleury noted that as a result of these two proposed rule changes, the nature and magnitude of pension liabilities might only become more difficult for those outside of the industry to understand.

Interface with State Street Retiree Services Complete – Mr. Fleury reminded the trustees that they had been informed a few months earlier of MECRS' updating of the method in which it performs pension payments and lump sum distributions through Retiree Services at State Street Bank. A local application known as NBX which batches information in the MECRS server was to be replaced with an internet application called PLUS Web which would allow MECRS staff to work directly on State Street System thus eliminating the maintenance associated with the local batch programs and giving staff immediate access to tax forms and cleared checks. The new application also allows MECRS staff to place stop payment on checks which had been issued and to track the status of such transactions on demand. Mr. Fleury was pleased to report that MECRS staff had successfully completed training during July, implemented processes and that MECRS was now operating on the new system.

Lexington Capital Calls - Mr. Fleury reported that Lexington Partners IV has notified investors of the next capital call scheduled for the following day, of which MECRS share would amount to approximately \$48,000.

Gottex Investor Conference Call - Mr. Fleury informed the trustees that Portable Alpha Manager, Gottex, had conducted an investor's conference call on July 31st, to summarize second quarter activity in the fund and to provide their vision for the second half of the year. One interesting theory which they put forth speculated that program trading, exchange traded funds and other computer related trading activities have combined to place lower quality securities in lockstep with the general market direction. Mr. Fleury noted that this makes the task of realizing value by the use of bottom up strategies more difficult because relative value is being swept aside in favor of general market momentum. He noted that he had reported this to NEPC and requested their opinion on the subject.

August 10, 2010
Minutes #462

Minutes of the Board of Trustees' Meeting -3-

Opal Financial Conference – Public Funds Summit East - In concluding his report, Mr. Fleury briefed the trustees on his attendance at the 2010 Opal Public Funds Summit in Newport, Rhode Island on July 21st, 22nd and 23rd. He noted that he had moderated a panel on investments in Real Assets at the conference and that a CD of all of the presentations made during the conference including information on the participating firms and biographies of the presenters is available to any interested trustees.

While on the topic of conferences, Mr. Fleury requested permission from the trustees to attend a similar conference scheduled for October 18th, in Boston, MA hosted by Information Management Network (IMN). He noted a number of items of interest on the seminar agenda, urged any interested trustees attend and promised to provide further details as they became available.

The trustees granted permission for Mr. Fleury to attend the conference on October 18, 2010.

Previous Business:

Accept and Place on File the final version of 2009 Required Auditors Communication and Auditors Report as Required by Governmental Auditing Standards - Trustee Porter moved to accept and place on file the final version of the 2009 Audit Communication and Audit Report.

Mr. Fleury noted that in the Required Auditors Communication packet included in the trustees' agenda, on the 3rd page, the reference to the date of the Management Representation letter was intentionally left blank. He explained that there was no date because there was no management letter written. A management letter was not drafted due to the lack of audit observations. The auditors observed that the one observation from two years ago had been corrected, they had not detected anything which merits an observation for this year and that MECRS was in compliance with the audit.

Trustee Porter commented that the MECRS staff should be commended for a job well done.

Status Report on Legislative Housekeeping - Mr. Fleury updated the trustee's on the status of proposed amendments to the MECRS death benefit provision. He explained that some time ago the MECRS Board had granted permission to workshop refinements to the death benefit provisions. After a review of the statute that had been in place for many years, it had been found to be incomplete and potentially problematic. Those issues having been identified, amendments were drafted with the assistance of legal counsel and the actuary. Mr. Fleury noted that the amendments were carefully crafted to ensure that they would be cost neutral the city. After the trustees review of the final draft of the LSR version, included in the trustee's agendas, Mr. Fleury noted that the next step would be to seek sponsorship concurrent with the notification of

Minutes of the Board of Trustees' Meeting -4-

the System's intent to the Manchester Board of Mayor and Aldermen to seek changes in the 2011 session of the legislature.

Trustee Sanders asked Mr. Fleury if he had documentation from the Systems Actuary confirming that there will be absolutely no cost impact to the City.

Mr. Fleury replied that he does have confirmation from the actuary and that he will forward that information to the Board of Mayor and Aldermen.

Chairman Pinard inquired as to where on the agenda, the trustees would be able to find notification of a death benefit payout.

Ms. Sandi Aboshar, Executive Assistant replied that unlike the Request for Retirement list of members retiring, provided to the trustees, an active deceased members payout would be found in the Refund Reconciliation Report under Consent Item #8 on the trustees agendas.

Chairman Pinard requested that Attorney Rich explain the provision changes made within the MECRS death benefit.

Attorney Rich summarized the death benefit provisions, noting each change made to the in-service death benefit as well as to the ordinary death benefit.

Mr. Fleury explained that the underlying theme to all the housekeeping amendments made to the death benefit provision was to assure income continuity to the family, while leaving the right of the member to provide that protection to their family, intact. With that task accomplished, it had come back before the board so that they would be fully aware of its status but that no further vote was required unless the trustees wished further amendments.

There being no further questions or comments on legislative amendments, Attorney Rich took the opportunity to move from the housekeeping measure to another legal matter. He informed the board that the McLane Law Office had been contacted recently by an attorney who indicated that a divorce marital master had issued an order to the parties in the divorce case that had joined the Retirement System into divorce litigation. Attorney Rich reiterated the System's current law, that if a member gets divorced, they cannot assign a portion of their benefit to their former spouse. Unlike the State Retirement System, the MECRS law does not provide for QDRO's. Correspondence had previously transpired back and forth from the MECRS to the divorce attorney regarding the issue. Apparently, counsel to the member did not adequately inform the court of the existing statute and the court subsequently issued an order dividing the member's benefit.

August 10, 2010
Minutes #462

Minutes of the Board of Trustees' Meeting -5-

Attorney Rich further reported that the member's new attorney objected to the court order and in response to that objection, the court issued an order requiring the Retirement System to be

brought into litigation. Attorney Rich stated that he drafted a letter to the new attorney explaining why the Retirement System does not have the ability to follow the order. He hoped that this correspondence would be helpful to the member's new attorney who had planned to ask the court not to include the Retirement System in the litigation. Attorney Rich reported that he will keep the board apprised of further developments regarding this issue should they occur.

Consent Agenda:

Chairman Pinard asked if any of the board members wished to remove anything from the Consent Agenda for discussion.

Trustee Hungler commented that he would like to remove item #C7.

Trustee Molan moved to accept the remaining consent agenda items, seconded by Trustee Sanders and passed unanimously by all those trustees present.

Regarding item #C7, Refund & Rollover Reconciliation Report, Trustee Hungler asked why the plan participants' social security numbers were included in the report.

Ms. Aboshar, Executive Assistant replied that the particular report in question was used for the first time due the misfiling and temporary unavailability of the report customarily used for this purpose. She went on to assure the board that in the months to follow the customary reports will be used, avoiding an unnecessary display of the member's Social security number.

Having availed themselves of the information on which to base a decision, the trustees systematically returned their Refund & Rollover Reconciliation Reports to the staff for destruction by confidential means.

It was then moved by Trustee Hungler and seconded by Trustee Molan to accept Consent Item #C7. Motion carried.

The Executive Director then stated for the record, that all correspondence inclusive of a member's private information is boxed consigned to Northeast Records Retention which picks up and disposes of such confidential information on a regular basis.

Minutes of the Board of Trustees' Meeting -6-

New Business:

Hedge Fund Managers Review – Mr. Kevin Leonard, Senior Consultant and Mr. Sebastian Grzejka, Senior Analyst were present to review and coordinate two Hedge Fund of Fund Manager presentations. The two managers had been invited to discuss performance to date and to brief the board on their outlook for the coming year.

Mr. Leonard began by ushering in Mr. John Boles, Client Service Director from Attalus Capital.

Mr. Boles started his presentation by providing a brief overview of Attalus Capital for those trustees that were new to the MECRS Board. He stated that Attalus is a Hedge Fund of Funds

based in the city of Philadelphia and founded in 1998. He also noted that Attalus is 100% institutional, with over 145 clients and approximately \$2.7 billion in assets under management.

Looking at the period of 2008, which Mr. Boles described as “a very difficult time in the markets”, he stated that Attalus did not lose a single client. Attalus was cash flow positive in 2008, remained so in 2009 and continued to be in 2010. He informed the board that Attalus lost 5 clients in 2009, primarily due to liquidity issues. The funds were returned to all investors seeking liquidation well in advance of the terms of the offering memorandum.

Referring to Tab II of the presentation booklet included in the trustee's agenda packets, Mr. Boles informed the board of some refinements or enhancements to Attalus' investment structure. He noted that the fundamental practice remains the same of not separating operational and investment due diligence on the clients behalf.

Mr. Fleury expressed concerns about recent press releases regarding new financial regulations coming in to play. He asked Mr. Boles to what extent might those regulations impact the hedge fund industry and particularly, Attalus.

Mr. Boles responded that he believed the regulations will have very little impact on Attalus Capital. The regulations will have more impact on commercial banks, investment banks and merchant banks.

Mr. Leonard asked Mr. Boles to speak on the ownership structure of the firm.

Mr. Boles informed the trustees that the ownership structure is held by both Patrick and Michelle Egan. He also noted that he owns a ½% of the firm and Anna Lui, Portfolio Manager also owns ½% of the firm. This year, he noted, that 3 or 4 additional partners will be added to the firm.

August 10, 2010
Minutes #462

Minutes of the Board of Trustees' Meeting -7-

Next, Mr. Boles turned the trustee's attention to pages 2 and 3 of his presentation booklet, noting that all the performance data is net of all fees and expenses and is audited through December 31, 2009. He reported that the cumulative return for the MECRS is 11.4% which represents a significant outperformance over the traditional equity markets with the annualized return of 2.01%.

Mr. Boles then referred to page 4 of the presentation booklet which provided a historical breakdown of the allocations by strategies between, total relative value, total event driven, total tactical and equity long/short. The chart on that page highlighted the quarter by quarter changes that Attalus made and illustrating the fact that they are active in the portfolio within the various strategies.

Mr. Leonard asked Mr. Boles how many underlying funds there are and what the turnover has been.

Mr. Boles answered that there are approximately 50 managers today within the portfolio with roughly a 15 to 20% turnover rate across the board, but primarily in the event driven category.

Mr. Boles noted that from a liquidity prospective, 80% of the multi-strategy fund is marketable securities, which can be liquidated without a penalty, given a 90 day notice. Approximately 8% of the entire portfolio is deemed illiquid securities.

Mr. Boles continued by stating that, Attalus has acquired roughly 10 new clients in 2010 and \$230 million in new subscriptions. He also stated that he was very proud to announce that there were no full client redemptions in 2008 and he attributed that to the stability of the firm.

From a personnel perspective, Mr. Boles informed the trustees that an additional analyst will be added to the firm this year, and will be joining the firm in September. Furthermore, he stated that there were other new hires to the investment team and client service staff, pending in 2010. The 2010 departures from Attalus include one client service director, who decided to return to the consulting world and also lost two junior analysts, who decided to pursue other careers.

Mr. Boles stated that for every three funds in which Attalus invests, the firm has one analyst covering those funds. Attalus is built to deliver consistent, stable performance. He also touted the "Attalus Mosaic" and integrated approach.

In concluding his presentation, Mr. Boles thanked the trustees for their continued support and the opportunity to review the fund.

Minutes of the Board of Trustees' Meeting -8-

Moving on to the next scheduled presentation, Mr. John Marshall, Partner & Director of Client Services and Mr. Joseph Pignatelli, Partner & Co-portfolio Manager both of The Archstone Partnerships, introduced themselves and began their review.

Mr. Marshall provided an overview of the firm's history, noting that Archstone Partners, L.P. began investing on January 1, 1991 with the idea of creating a portfolio of hedge funds that would provide long term growth of capital, with low volatility. He noted that the total assets under management currently is \$4.6 billion, all in fund of funds, with 62% being institutional and 38% being private clients. He then referred to a Representative Institutional Client List on page 37 of the presentation booklet.

Mr. Marshall stated the investment objectives of Archstone Offshore Fund, Ltd have not changed since inception in 2000. In general those objectives are, to protect capital during declining markets while participating during market advances, to seek to build capital by earning a premium of 600 basis points over the risk-free rate (treasury bills) over the course of a market cycle, to achieve the returns with low volatility, and to minimize the possibility for capital loss.

Next Mr. Marshall turned the trustee's attention to page 11 of the presentation booklet, Performance Analysis, as of June 30, 2010. He reported that through July, 2010, Archstone is up 93 basis points and also that many of Archstone's managers were able to take advantage of the lower volatility earlier in the year by using "out of the money puts" to protect downside risk.

Mr. Marshall referred to page 7 of the booklet. In terms of portfolio exposure, he referred to the pie chart which showed that equity exposure was higher than the cash exposure which he said is indicative of the conservative position of Archstone's managers. Turning to the next page, he addressed chart of "historical exposure" gross. Net, long and short which has gradually recovered from the depths of the crisis in 2008.

Mr. Leonard asked Mr. Marshall to speak to the organization of the firm, the research and the function of the organization.

Mr. Marshall had the trustees flip to page 26 of the presentation booklet. He noted that Fred Shuman and he are the portfolio managers. The research group is lead by Mark Smith in addition to three analysts. The analysts are assigned to about 10 managers and their job is to keep the portfolio managers updated on the day to day issues regarding their clients. He then listed the operations due diligence group as well as their procedures within Archstone.

Mr. Leonard requested that Mr. Marshall speak to the ownership structure of Archstone.

August 10, 2010
Minutes #462

Minutes of the Board of Trustees' Meeting -9-

Mr. Marshall replied that Fred Shuman owns the bulk of Archstone with Capital Partners, Stan Shuman, Richard Nye, and Steve Kotler. They are in the advisory capacity and have no operational involvement of the firm. He noted that profit participation is then acquired on the basis of longevity within Archstone.

Attorney, John Rich asked Mr. Marshall, Since there has not been any turnover within the investment professionals, what did the partners learn in 2008 that they can put to work to prevent a similar decline in asset values from happening again?

Mr. Marshall replied, that Archstone acted like a principal, not like an agent and that 2008 validated philosophy and strategies they had adopted from inception.

The other lesson learned from 2008, Mr. Pignatelli added, is that Archstone has always paid attention to the philosophy and the liquidity issues have always matched Archstone's strategy.

Mr. Marshall and Mr. Pignatelli thanked the board for their time and departed.

Mr. Leonard expressed his opinion that in comparing presentations, Archstone had delivered a more in-depth review of their fund.

Mr. Leonard noted that Attalus Management is a multi strategy manager and a core fund of funds with beta exposure. He further stated that one of NEPC's concerns with Attalus is their ownership structure. Attalus is run by a husband and wife team who lack interest in spreading ownership of the firm. By comparison, Mr. Leonard noted that Archstone has extended meaningful ownership of their firm. Another concern with Attalus, Mr. Leonard cited, is that the research group with Attalus conducts the operational due diligence as well as the manager research, performance evaluation. He expressed concerns over whether Attalus is thorough in their process.

Mr. Leonard pointed out two positive issues regarding Attalus Capital, the firm is opening up an international office overseas and, they have new analyst joining the firm. He stated that NEPC will continue to monitor those developments in the coming months.

Attorney Rich asked Mr. Leonard, how many of the hedge fund of fund managers are on NEPC list of recommended managers.

Mr. Leonard replied that there are 30 to 40 managers on the list and approximately ten of them are recommended.

He informed the trustees that while neither Attalus nor Archstone are currently on NEPC's recommended list, that NEPC is not recommending that the trustees terminate their contract with

Minutes of the Board of Trustees' Meeting -10-

them. It was also noted that Archstone and Attalus were hired prior to NEPC's engagement with the System.

Attorney Rich asked Mr. Leonard, why Attalus is not NEPC's recommended list and wondered if it was due to performance and ownership issues.

Mr. Leonard replied that Attalus is not on the list due to the qualitative aspects of the firm and the fact that the returns, while adequate, could be instead be higher.

Having concluded presentations and discussion related to Hedge Fund of Fund Managers, Mr. Sebastian Grezjka of NEPC opened the review of the Investment Performance Analysis, distributed to the trustees which covered second quarter returns.

Mr. Leonard gave a brief update of market performance noting that S&P 500 had been up 7% for the month of July with the EAFE was up 9.5%, and fixed income, up 1.1% which was a reversal from the results at the end of June.

Mr. Leonard turned the trustee's attention to page 29 of the Investment Performance booklet and provided them with a review of total fund performance from the flash report. He pointed out universe comparisons such as domestic equity on a year to date basis. He further noted that the

Russell 3000 is down 6% and the overall domestic equity composite, down 4.1%. Benchmark Large Cap + Alpha was down 4.2% outperforming the S&P 500 which is down 6.7% but Gottex, has lagged the S&P year to date. He reported that Pzena is down 4.3%, but in comparison to other similar managers in the large cap value space, they rank in the top quartile. He also reported that small cap stocks have done well, the S & P 500 on a year to date basis is flat at negative 10 basis points and international is still the worse reporting asset class down 5%. Rothschild on a year to date basis, down 90 basis points, ranked in the 34th percentile.

The international equity portfolio, he continued, is doing very well. Managers Gryphon and Causeway are both doing well versus the benchmark and peer groups, and City of London outperforming the emerging markets benchmark.

Mr. Grzejka took over the presentation, stating that core bond manager Income Research and Management reported year to date returns up 5.6% placing them in the 39 percentile. Over the last 3 years, IRM returned 8.5% versus 7.5% for the benchmark. Loomis Sayles had a negative quarter which had a lot to do with underlying exposure and tolerance for risk. Seix Advisors was slightly positive for the quarter but lagged their benchmark for both the quarter and year to date.

August 10, 2010
Minutes #462

Minutes of the Board of Trustees' Meeting -11-

After hearing the returns for Seix Advisors, Mr. Fleury cited news regarding the pending sale of Seix Advisors which the board had addressed at a previous meeting and he added the more recent events resulted in the departure of two employees from within the firm.

Mr. Grzejka stated that NEPC will continue to track the changes with Seix Advisors however, he indicated that NEPC does not anticipate the changes affecting the investment processes associated with the portfolio.

After brief discussion on various asset classes and the anticipated returns within the MECRS portfolio there were no further question from the board. Mr. Leonard and Mr. Grzejka thanked the trustees for their time and departed.

Motion to Adjourn:

Having concluded all of the items of business for the day, Chairman Pinard entertained a motion to adjourn. Trustee Porter moved to adjourn at 11:13 a.m. seconded by Trustee Molan and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard E. Fleury
Executive Director