August 9, 2011
Minutes #473

Minutes of the Board of Trustees' Meeting -1-

Call to Order: Chairman Pinard called the meeting to order at 8:30a.m.

Present: Trustees: Chairman Pinard, Paul Porter, Richard Molan and Michael Woitkowski and Dianne Mercier arrived at 8:40 a.m.

MECRS Staff: Gerard Fleury, Sandi Aboshar and Suzanne Wilson

Absent: Trustees: William Sanders and Mayor Ted Gatsas

In Attendance: Attorney John Bentas of the McLane Law Firm, Kevin Leonard and Sebastian Grzejka, Advisors from NEPC, and Joseph Pignatelli and John Marshall, both Partners of The Archstone Offshore Fund. Also in attendance were MECRS Members, Fred Turner and Edward Couture accompanied by his wife Lynne Couture

Approval of the Minutes of the Previous Board Meeting July 12, 2011:

Trustee Molan moved to approve the minutes of the meeting of July 12, 2011 seconded by Trustee Porter and passed unanimously by all trustees present.

Approval of the Immediate Meeting Agenda:

A motion was made by Trustee Molan to approve the immediate meeting agenda, seconded by Trustee Woitkowski, and the motion carried.

New Business:

Requests for Ordinary Disability - Fred Turner and Edward Couture – Mr. Fleury referred to his Summary Recommendations included in the Trustees agenda packets. He reported that both applicants, Mr. Fred Turner and Mr. Edward Couture have met all of the requirements pursuant to Chapter 218:15 Laws of 1974, as well as Administrative Rule Section 2.3 for their disability requests. As a result of meeting both the statutory and regulatory requirements, Mr. Fleury recommended in both cases that the board look favorably on their respective requests for Ordinary Disability Retirement.

Trustee Molan announced that in the case of Mr. Edward Couture, he would like to recuse himself, owing to the fact that Mr. Couture is a member in a bargaining unit which he represents.

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Mr. Fleury noted that the lack of Trustee Molan's vote would cause the group to drop below quorum requirements. He therefore suggested that in order to avoid the quorum issue, that Trustee Molan's disclosure be shown for the record as an appearance of a potential conflict of interest but that he be allowed to vote on the question.

It was then moved by Trustee Porter to approve Mr. Fleury's recommendation for Ordinary Disability Retirements for Fred Turner and Edward Couture, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Acceptance of Gainful Occupation Report for 2010 - Trustee Porter moved to accept and place on file the report of Gainful Occupation for 2010, seconded by Trustee Woitkowski and passed by all those trustees present.

Report of the Executive Director:

Progress Report on PTG Project - Mr. Fleury began by reporting that work is going well with the Pension Technology Group project. MECRS staff is now able to write queries against the new database and quickly summarize data in ways never before possible. Weekly conference calls continue and MECRS is on track for implementation of the new system by fall.

Increase in Trustee Mileage Reimbursement Rate – Next, Mr. Fleury informed the trustees that the mileage rate to and from board meetings has been increased by the IRS to 55.5 cents per mile from 50 cents beginning July 1, 2011.

Attendance at Public Funds Summit East - Mr. Fleury thanked the board once again for allowing him to attend the Public Funds Summit-East in Newport, RI on July 18, 19, & 20. Mr. Fleury reported that as usual there had been a wealth of information from fund managers, investment advisors, actuaries, and of course, peer public funds administrators and trustees. Mr. Fleury informed the trustees that he has a CD available, of all the information and presentation materials addressed over the three days. He speculated that the single and most relevant topic worthy of further tracking is the staggered implementation of provisions of the Dodd-Frank Wall Street Reform & Consumer Protection Act. In particular, current reporting requirements for public funds with holdings offshore may be rescinded and new requirements on transactions may affect how hedge fund and portable alpha managers operate.

Status of Manager Changes – Moving on, Mr. Fleury noted that the manager contracts in the amount of $6.5 million with Standish and $6.7 million with Permal were completed for funding August first. Considerable assistance was provided by legal counsel at the McLane firm in order to make the August deadline. The Investment Management Agreements, (IMAs) provided by each of the mangers were better structured for entities other than public plans and that added to the challenge. In addition, there were some provisions which MECRS wanted to add to those agreements in order to better protect its interests and some terms which required clarification and amendment before things could proceed. Mr. Fleury was pleased to report that in the eleventh hour, with a high level of cooperation by all involved, the necessary amendments were completed and the deadline was met.

Archstone Partnership Review - Chairman Pinard called upon Mr. Kevin Leonard and Mr. Sebastian Grzejka from New England Pension Consultants to introduce representatives, Joseph Pignatelli, President & Co-Portfolio Manager and John Marshall, Managing Director of Client Services from the Archstone Fund.

After brief introductions, Mr. Marshall directed the trustees' attention to page 3 of a presentation booklet which had been included in their agenda packets. Mr. Marshall provided the trustees with a brief overview of the firm, noting that it had begun investing on January 1, 1991. Mr. Marshall noted that total assets under management by the firm approximate $4.8 billion, with 60% coming from institutional clients and the remaining 40% coming from private clients.

Mr. Marshall noted that the investment objectives of Archstone Offshore Fund, Ltd. have not changed since that fund's inception in 2000 and he went on to list those investment objectives.

Referring to a pie chart on page 5 of the review booklet, Mr. Marshall reported that there are currently19 hedge fund managers within the Archstone fund of funds portfolio and that over the last ten years, the range has varied between 18 to 26 managers. The target allocation since inception has been 60% to long/short hedge equity managers and 40% to the Non Directional Absolute return, with the objective of maintaining a portfolio that would do well regardless of the market environment.

Mr. Marshall indicated that unlike Archstone's competitors, Archstone does not impose the market view on the portfolio and he cited that as a factor which differentiates them from the others. He went on to note that no more than 10% of the portfolio is allocated to any single manager. All of the managers have common characteristics which give insight into Archstone's investment philosophy. Elaborating further, Mr. Marshall stated that most of the managers have at least 50% of their net worth of their own funds invested and in many cases they are the largest investor in their own fund, a practice known as Agency Theory. Archstone believes that the Agency Theory philosophy is a big motivator as well as a big controller of risk.

Mr. Marshall continued listing other common characteristics in Archstone's investment philosophy.

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Next, Mr. Marshall addressed the strategies that Archstones managers were invested in as of July 1, 2011. He described the strategies as changing dynamically in real time at the manager level and he described how that strategy works.

Moving on, Mr. Marshall provided a description of the Archstone Offshore Fund's historical investment exposure by geographical sector.

Mr. Marshall recounted MECRS's account performance since investing in the fund. He also provided a performance analysis as of June 30, 2011 and noted that year-to-date through July 31, 2011, the fund is up 1.08%.

Mr. Leonard asked Mr. Marshall if the performance numbers were net of fees or gross of fees.

Mr. Marshall replied, that the performance results are net of fees.

Mr. Marshall explained that basically for the latter half of 2009, all of 2010, and the first quarter of this year, MECRS' portfolio had operated in recovering and up trending markets. He noted that successful investors know how critically important it is to avoid large losses in order to achieve investment success. Mr. Marshall closed by stating that Archstone's goal is to protect on the down side while participating on the up side, and he turned the presentation over to Mr. Pignatelli, Managing Director of Client Services.

Mr. Pignatelli stated that he currently believes that bond markets continue to function well, as do the equity markets. Market concerns appear to reside at the government level not at the financial system level. Financial institutions in general are well capitalized so the issues revolve around government policy and debt, rather than corporate.

Futher elaborating on investments in equities, Mr. Pignatelli commented that equity investors today, are in the best financial shape, with cash in the balance sheets and it is likely that they are going to continue and accelerate buyback programs.

Trustee Mercier expressed concern about Mr. Pignetelli's optimistic opinion of the equity markets. She noted that in 2008 the federal government injected considerable liquidity into the economy, a feat which it cannot easily repeat. Her concern was that absent the ability to intervene a second time, the general picture for equities might not be so rosy.

Mr. Pignatelli referred to a pie chart of strategy exposures and reiterated Mr. Marshall's earlier comments.

After providing a brief update on Archstone's personnel, Mr. Marshall briefed the trustees on the existence of a new share class offered to all of the offshore funds as of July 1, 2011. The option

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consists of changing to a 1% management fee with a 5% set up fee. Transition to the new class can be made on a quarterly basis, with a 30-day notice, and Mr. Marshall offered it for the trustees consideration. Because the implications of the offer were not conspicuous, Mr. Leonard was asked whether this option would be advantageous to MECRS.

Kevin Leonard stated that NEPC would look into the option and provide a recommendation to the trustees at a future meeting.

Mr. Marshall and Mr. Pignatelli having concluded their presentation and there being no questions from the board, they thanked the board for their time and departed at 9:10 a.m.

Chairman Pinard asked the NEPC representatives to begin their performance summary for the second quarter.

Mr. Leonard began by distributing booklets entitled Private Markets Review and Investment Performance Analysis. He then began to elaborate on what has transpired over the last week in the markets as well as the outlook for the overall markets. He noted that the Standard & Poor's downgrade of the US Sovereign credit rating from AAA to AA+, along with evidence of slowing global growth and the deepening European debt crisis had led to significantly increased market volatility.

He informed the trustees that NEPC is recommending that their clients maintain their disciplined approach to investing and he noted that while NEPC is not advocating major tactical changes in the short-term, some steps to consider in the coming months include: reviewing investment guidelines, re-considering the risk in the portfolios and to consider re-balancing toward targets.

Referring to the Second Quarter 2011NEPC Observations and Opportunities page contained in one of the handouts, Trustee Mercier asked Mr. Leonard to explain, taking on reasonable exposure to illiquidity.

Mr. Leonard explained that NEPC views public pensions as a provider of liquidity. He noted that the MECRS portfolio has taken advantage by taking part in the recommended opportunities in the current market environment. He further explained that because of the way the plan is structured, MECRS's has the ability to take a little bit higher volatility risk in its portfolio.

Mr. Leonard continued by providing the trustees with a comparison between the market back in 2008 and the current market landscape. He noted that according to the experts, conditions now present a buying opportunity. Mr. Sebastian Grzejka continued NEPC's presentation by calling the trustees attention to the Investment Performance Analysis Booklet and recapping the board's recent decisions and activities including the decision to replace Attalus Capital with Permal. Permal has a fixed income bias which pairs very well with Archstone. Archstone has the equity long/short bias, so overall; the portfolio provides a nice balanced allocation.

To round out the fixed income part of the portfolio following the Emerging Market Debt Managers interviews, Mr. Grzejka reminded the board that Standish Capital had been chosen to fill the new mandate.

Lastly, RMK Timber had been able to liquidate a portion of assets in that fund through the sale of underlying properties, and he noted that the sale is reflected in MECRS's recent performance.

Mr. Grzejka then addressed ongoing activities and noted that NEPC is preparing a 2011 private equity plan for the portfolio and would be providing an education update on Real Estate, subsequent to making a recommendation to the asset class during the second half of 2011.

In terms of the asset allocation, Mr. Grzejka referred to page 23 of the booklet, breaking down a chart of the policy target allocation, actual manager allocation and net asset class exposure.

Mr. Grzejka noted that one year ago the MECRS's total portfolio value was $124 million. As of June, 2011, with net external growth of $2.5 million and return on investments $27.5 million, the MECRS's portfolio market value was now $154 million.

Mr. Grzejka summarized the total fund performance and strategies of each asset class as well as future opportunities and expectations.

Mr. Fleury asked Mr. Leonard whether he had any short term advice for the board in the event that RMK might liquidate the balance of the Timber Investment. Mr. Leonard replied that NEPC, from a planning standpoint, believed that October would be a good time to have the 2012 planning session for private equity. If RMK liquidations occur before then, then the funds could be temporarily placed somewhere else in the portfolio.

Mr. Fleury then asked the NEPC representatives, if they were aware that Newstone Capital had approached all of their investors with a very broad Most Favored Nations Offering consisting of 139 items?

Mr. Leonard replied that he would research the MFN question and report back to Mr. Fleury, later in the day.

The NEPC representatives having completed their presentation and there being no further questions of the board, Mr. Leonard and Mr. Grzejka thanked the board for their time and departed.

Report of the Investment Committee:

Committee Chairman Molan noted the outstanding job done by the McLane legal counsel in reviewing and completing the Investment Management Contract with Permal Asset Management in time for the August investment deadline.

Consent Agenda:

Trustee Molan moved to accept the Consent Agenda seconded by Trustee Porter and passed unanimously by all those trustees present.

New Business:

Most Favored Nation Status Options - Newstone - Attorney John Bentas of the McLane Law Firm began by introducing himself and stating that due to Attorney John Rich's absence, he would be explaining the options made available to MECRS regarding the MFN Status of Newstone Capital, Partners.

First, Attorney Bentas provided a background of the Most Favored Nation Option Compilation explaining that Newstone Partners had a 15 month period where they were seeking investors. The provision in the governing document states that during that 15 month period, all side letters or provisions with other investors must be disclosed.

Attorney Bentas explained that with that 15 month period closing, the 139 provisions and side letters with other investors have been crafted. Of those 139, 39 are not available to all investors.

Those 39 provisions focus on investor specific requirements that are by statute or an investment policy of a particular investor.

Referring to the MFN Compilation, which had been included in the trustees' agenda packets, Attorney Bentas noted that McLane's methodology was to review them all and choose the ones that were at least of no net harm to the System. The recommendations were finalized after a meeting with Mr. Fleury and were now being submitted for adoption by the Board of Trustees.

It was then moved by Trustee Mercier to accept the recommendation of legal counsel and to adopt the slate of the MFN provisions, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Subsequent to the approval by the Board of Trustees', Chairman Pinard was asked to endorse the MFN Contract.

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Motion to Adjourn:

Having completed all of the items of business for the day, Chairman Pinard entertained a motion to adjourn. Trustee Molan moved to adjourn at 10:10 a.m. seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard E. Fleury
Executive Director

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