

June 14, 2011
Minutes #471

Minutes of the Board of Trustees' Meeting -1-

Call to Order:

Chairman Pinard called the meeting to order at 8:31 a.m.

Present:

Trustees: Chairman Pinard, Michael Woitkowski, Paul Porter, Dianne Mercier and Dick Molan
MECRS Staff: Gerard Fleury and Sandi Aboshar

Absent:

Trustees: William Sanders and Mayor Ted Gatsas

In Attendance:

Attorney John Rich of the McLane Law Firm and Mark LaPrade,
Principal at the audit firm of Berry, Dunn, McNeil & Parker

Approval of the Minutes of the Previous Board Meeting May 10, 2011:

Trustee Mercier moved to approve the minutes of the meeting of May 10, 2011 seconded by Trustee Molan and passed unanimously by all those trustees present.

Approval of the Immediate Meeting Agenda:

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

Report of the Investment Committee:

Investment Committee Chairman Molan reported that an Investment Committee Meeting had been held on June 13, 2011, at which time three prospective Fund of Funds Managers were interviewed. Chairman Molan noted that the MECRS Investment Consultants from NEPC were also present to assist in the interview process.

Of the three interviews conducted, Committee Chairman Molan reported that the Investment Committee is recommending that the full board, hire Permal Asset Management. That recommendation was based upon the company's structure & composition, its investment practices, its competitive fee structure, its total return for the one, three, five and ten year periods and its lack of any lock-up.

Committee Chairman Molan noted that funding for this replacement manager, approximately \$6.8 million, will come from the liquidation of the investment with Attalus Capital who was issued a termination notice in March of 2011.

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Committee Chairman Molan then offered a motion to hire Permal Asset Management, which was seconded by Trustee Woitkowski. Chairman Pinard called for the vote and the motion passed unanimously by all trustees present.

Previous Business:

Results of 2010 Audit and Delivery of Draft Audited Financial Statements for 2010 - Chairman Pinard introduced Principal, Mr. Mark LaPrade, of Berry, Dunn, McNeil & Parker who delivered the draft audited financial statements for 2010.

Mr. LaPrade began by referring to the draft Required Auditor Communications and the draft Financial Statements distributed to the trustees at the beginning of the meeting. Referring to the Financial Statements, Independent Auditors Report, Mr. LaPrade explained that the MECRS Audit was conducted in accordance with U.S. generally accepted auditing standards. Those standards require that the audit obtain reasonable assurance, not absolute assurance, about whether the financial statements are free of material misstatement. Mr. LaPrade explained that the audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

Mr. LaPrade went on to say that the audit does look at internal controls; however BDM & P is not issuing an opinion on the internal controls. Also Mr. LaPrade noted that the opinion on the financial statements is unqualified.

From qualitative aspects of accounting practices, Mr. LaPrade explained that there were no transactions identified where there is a lack of authoritative guidance or consensus and that all significant transactions have been recognized in the proper period.

Mr. LaPrade noted sensitive disclosures within the financial statements, the schedule of net appreciation (depreciation) of all the investments held for the year as well as the disclosures required by GASB 40 for the investments held as of December 31, 2010 and 2009 respectively. Mr. LaPrade also pointed out a chart indicating the increasing funded status of the Plan for the last two years.

Next, Mr. LaPrade addressed the significant accounting estimates which affect the financial statements. He identified them as the calculation of actuarially determined contributions, the actuarial accrued liability and actuarial value of plan assets which are disclosed in Note 8, the fair value of investments valued on a basis other than quoted prices (\$23.4 million at 12/31/2010 compared to \$22 million at 12/31/2009) and the allocation of financial statements amounts between the pension and health subsidy trusts.

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Mr. LaPrade reported that, from an audit adjustments standpoint, all of the adjustments recorded during the audit were provided by management therefore there were no audit adjustments identified during the audit process.

However, Mr. LaPrade continued by noting that BDM &P does have three unrecorded audit adjustments for 2010 regarding the timing of the City's contribution, the true-up and how that would flow through the current year's financial statements. He suggested that they might have been recorded by the Retirement System as a receivable or a payable. He explained that they are only .1% of the unadjusted increase in net assets however, and not material.

Regarding other required communications, the audit reported no difficulties or disagreements with management as well as no consultations with other accountants about auditing or accounting matters. Also, the auditors did not note any deficiencies in internal control that they considered to be a material weakness.

Mr. LaPrade stated that part of the audit requires that he inquire if the Board of Trustees has any knowledge of any instances or suspicions or allegations of fraud within the Retirement System.

The Board of Trustees did not report any concerns.

Mr. LaPrade then informed the trustees that as part of the audit process a two or three page Yellow Book Report will be issued to the System. The essence of the Yellow Book Report is broken down into two sections, internal controls over financial reporting and compliance & other matters where they did not identify any material control matters or any non-compliance matters that they would have been required to report.

In completing his presentation, Mr. LaPrade addressed the financial statement highlights noting that net assets increased by \$20 million in 2010 compared to \$22.5 in 2009. He also noted an increase in benefit payments due to an increase in the number of retirees in 2010 compared to 2009.

Referring to the MECRS Annual Report he noted changes in the Schedule of Employer Contributions for Pension Benefits and Health Trust on page 42 of the CAFR. Mr. Fleury stated that it is his understanding that the auditors recommend some indication that the City has in fact met its employer obligation each year, and that he intended to comply through the use of a footnote. Mr. Fleury reported that he has also forwarded the auditors comments to the System's actuary requesting an amendment in the actuary's future reporting format in order to avoid a repetition over this matter and he stated that he was pleased with the audit process.

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It was then moved by Trustee Porter to accept the draft audit results for 2010, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Consent Agenda:

Trustee Molan moved to accept the Consent Agenda for February, seconded by Trustee Mercier and passed unanimously by all those trustees present.

Report of the Executive Director:

Earnings Comparison Benchmark & Gottex and NEPC Conferene Call of May 13th - Mr. Fleury began by summarizing a conference call conducted on May 13th with NEPC representatives regarding Gottex's performance since inception. Mr. Fleury reported that in that call, NEPC Representative, Mr. Alex Kamunya had detailed NEPC's understanding of why Gottex had trailed Benchmark in their recovery from the 2008 declines which impacted most asset classes. As part of the discussions, Mr. Kamunya's noted that NEPC is no longer recommending Gotttex and has placed a neutral rating on them for existing investors. He cautioned however, that replacing Gottex at this time might be ill advised given their recovery rate and distance from the high water mark in their fee schedule. Mr. Kamunya indicated that AUM for Gottex had fallen from a high of \$15 billion to the present level of approximately \$8 billion which should make it easier for them to focus on return strategies rather than trying to adaquately allocate excessive AUM. He cautioned that if AUM should suddenly begin to increase in correlation with a decline in the rate of return, that the question of replacing the manager would need to be revisited.

Laws & By-Laws Reprinted - Mr. Fleury informed the trustees that updates to the MECRS Law Book and Summary Plan Description have been completed and are included in the trustees agenda packets as well as being posted on the MECRS website.

Progress Report on PTG Project – Mr. Fleury reported that work is going well on the PTG project. MECRS staff now has access to the new system and have been confirming elements of data conversion from the old system. Weekly conference calls to resolve problems have had few issues to resolve and steady progress is being made.

COLA Response from Retirees – Next, Mr. Fleury was pleased to share a “thank you” call from retiree Marie Varle in response to a notice issued to retirees of the pending COLA increase approved by the board at its May meeting.

Attendance of NEPC Open House & Client Conference - In closing his report, Mr. Fleury stated that on May 17th he was able to attend the NEPC Open House in Cambridge, tour their facility

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and meet back office staff who contribute to services supplied to MECRS. He also reported that the following day he attended a full day session of the annual NEPC Client Conference. The conference featured presentations on a variety of relevant topics and participants were able to see real time poll results of questions posed to the audience of NEPC clients. Those questions were designed to chart economic and market sentiment and revealed an interesting disparity between individuals and organization.

Report of the Benefits Committee:

Committee Chairman Porter informed the trustees of a Advisory Committee Meeting scheduled for June 16, 2010

Other Business:

Attorney Rich of the McLane Law Firm reported that MECRS is in the process of finalizing the contract with newly hired Manager, Standish Mellon, for an Emerging Market Debt – Local Currency mandate.

Attorney Rich also addressed progress to date in his discussions with the actuary pursuant to an April board directive to review the continued appropriateness of COLA Administrative Rule 7. Attorney Rich distributed a status report to the trustees and reported that on June 7, 2011 the System's Actuary and legal counsel discussed Administrative Rule 7 with Executive Director Fleury. All parties agreed that since Rule 7 was adopted prior to actuarial assumption changes and prior to the pre-funding of COLAs, Rule 7 should be updated.

Attorney Rich listed the different aspects of Rule 7 and the COLA processes which were reviewed during the conference call and listed alternatives for trustees consideration.

1. Presumption that COLA can be paid based on sufficient investment performance rather than funded status
2. Should there be a rule at all?
3. Should the Rule include presumptions of "sufficient earnings" and inflation?
4. Definitions of "sufficient earnings to allow a COLA award
5. Measure of inflation – CPI-U or other measurement
6. Should the level of earnings limit the amount of COLA?
7. Which retired members are eligible to receive a COLA?
8. How much of the lost purchasing power should the system be responsible for restoring and how much should be a member's responsibility?
9. Development of chart decision tree to facilitate decision making

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After lengthy discussion by the trustees and Attorney Rich on the history of the COLA Rule and the pre-funding of COLAs, Attorney Rich was directed by the trustees to conduct further research on the matter in collaboration with the System's actuary, Gabriel, Roeder, Smith & Co. and asked to report back to the board at a date to be determined.

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 9:45 a.m. seconded by Trustee Porter and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard E. Fleury
Executive Director