July 10, 2012
Minutes #483

Minutes of the Board of Trustees' Meeting -1-

Call to Order: Chairman Pinard called the meeting to order at 8:36 a.m.

Present: Trustees: Chairman Donald Pinard, Paul Porter, Richard Molan, William Sanders and Michael Woitkowski arrived at 8:48 a.m.

MECRS Staff: Gerard Fleury, Sandi Aboshar and Suzanne Wilson

Absent: Trustee Dianne Mercer, Mayor Gatsas

In Attendance: Attorney John Rich of the McLane Law Firm and Mark LaPrade of Berry, Dunn, McNeil & Parker

Approval of the Minutes of the Previous Board Meeting:

A motion was made by Trustee Sanders to approve the minutes of June 12, 2012, 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 Sanders, and passed unanimously by all those trustees present.

New Business:

Results of 2011 MECRS Audit - Chairman Pinard introduced Principal, Mr. Mark LaPrade, of the accounting firm, Berry, Dunn, McNeil & Parker, the System's outside auditor who delivered the draft audited financial statements for 2011.

Mr. LaPrade began by referring to the Executive Summary distributed to the trustees, inclusive of Required Auditor Communications, Yellow Book Report as well as the draft, Comprehensive Annual Financial Report. Beginning with 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 stated that the audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements and assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

Mr. LaPrade indicated that the audit does look at internal controls; however Berry, Dunn does not issue an opinion on 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 indicating a lack of authoritative guidance or consensus and that all significant transactions have been recognized in the proper period.

Referring to the Comprehensive Annual Financial Report (CAFR) 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, 2011 and 2010 respectively which can be found in Note 3. Disclosures also include the funded status of the plan, which is highlighted in Note 8 of the CAFR.

Mr. LaPrade noted that there were no adjustments to the financial statements as a result of the audit process; however there were three unrecorded audit adjustments for 2011, similar to those in the prior year, which had to do with the true-up.

Mr. LaPrade listed the unrecorded adjustments:

- To record the impact of the actuarially calculated underpayment of employer contributions for the applicable City departments for the period of July 1, 2012 and June 30, 2011.

- To record the estimated impact of the difference between the projected and actual payroll for the applicable City departments for the period of July1, 2011 through December 31, 2011.

- Reversal of prior year unrecorded adjustments that impacted the 2011 financial statements.

Chairman Pinard asked Mr. LaPrade if the payroll estimate has been higher or lower than actual.

Mr. LaPrade replied that historically, the number has gone both ways, but in 2011 the payroll estimate had been lower than actual, resulting in an additional obligation by the City.

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. Other significant accounting estimates include, 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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Trustee Sanders interjected that 2 years ago, there was a higher estimated payroll than actual and this year a true-up payment was made by the City to the Retirement System in the amount of $520,000, because last year the estimate was lower.

Moving on, Mr. LaPrade reported on the required supplementary information and noted that "limited procedures" were applied to the supplementary information. Berry Dunn does not provide an opinion on the Required Supplementary Information, only a review. He also reported that there were no difficulties or disagreements with management in performing the audit.

Mr. LaPrade stated that the audit did not note any deficiencies in internal controls that were considered to be a material weakness.

Next, Mr. LaPrade asked the Board of Trustees if they were aware of any instances of allegations of fraud.

The Board of Trustees did not report any concerns.

In completing his presentation, Mr. LaPrade provided the trustees with a summary of the "Yellow Book Report", internal control over financial reporting and stated that the audit did not identify any control matters that would be considered to be a material weakness. Also, Mr. LaPrade stated, that from the compliance perspective, it has been noted that there were no instances of noncompliance or other matters that would be required to be reported.

It was moved by Trustee Porter to accept the MECRS 2011 CAFR, seconded by Trustee Molan and passed by all those trustees present.

The trustees thanked Mr. LaPrade for his presentation, to which Mr. LaPrade thanked the trustees and departed.

Chairman Pinard then recognized the MECRS staff for their efforts which he attributed to the favorable audit reports.

Report of the Executive Director:

Problem with Custodial Services - Mr. Fleury reported that there was a meeting held June 29th with a representative from State Street Public Funds Services, to discuss reporting delays experienced in the past few months. Likely causes for those delays were identified and MECRS has been given assurances that the problems will not occur again.

MECRS 2012 Pre-Retirement Seminar now Scheduled for September 11th - Mr. Fleury commented that thanks to the board's indulgence in changing its usual meeting date, the 2012 MECRS Pre-Retirement Seminar has been scheduled for Tuesday, September 11th at the

Executive Court. Speakers from the Social Security Administration and other retirement relevant organizations have already committed to presentations and registration will begin in the

coming weeks. He then noted that the September MECRS Board of Trustees meeting will be held on Tuesday, September 18, 2012.

Status of Real Estate Manager Consolidation - In closing his report, Mr. Fleury noted that at the end of the first quarter of 2012, the board elected to terminate real estate manager Morgan Stanley and to award the proceeds to Prudential Real Estate. Redemption notices were prepared and sent to Morgan Stanley to become effective at the end of June and MECRS was enrolled in Prudential's entry queue. As of the end of June, 90% of the Morgan Stanley proceeds had been received with the remaining balance due within ten days and slightly more than one quarter of the new commitment to Prudential had been called and funded.

Report of Investment Committee:

Committee Chairman Molan reported that at the MECRS, Investment Committee meeting held in June, three potential Investment Managers were interviewed as prospective diversifiers to the Global Tactical Asset Allocation segment of the portfolio. He noted that prior to the start of today's board meeting; the Investment Committee convened a session to further discuss those interviews held in June and to formulate a recommendation for the full board's consideration.

Committee Chairman Molan stated that it is the Investment Committee's recommendation that the board select PIMCO "All Asset Fund" to supplement Mellon, at a percentage to be determined by NEPC and the executive director. Committee Chairman Molan reported that PIMCO should provide downside protection to the GTAA investments, with low volatility of approximately 15%. In addition, he cited PIMCO's impressive overall administrative support and research capabilities.

It was moved by Committee Chairman Molan to select PIMCO to supplement Mellon, seconded by Trustee Sanders and passed unanimously by all those trustees present.

Committee Chairman Molan then reported on the Investment Committee's second recommendation to amend the MECRS Investment Guidelines & Objectives, by adding a section which would allow the trustees to invest with managers who utilize exchange trade funds.

Mr. Fleury explained to the trustees that the amendment would add a new section 8 to page 5 of the existing rules. The text of the section would read: "The use of exchange traded funds (ETF's) is permitted in the portfolio, so long as is within the parameters of the guidelines listed above. It is understood that an allocation to ETF's is meant to represent broad market exposure via an individual security, therefore, any allocation that falls outside of the parameters of these guidelines requires prior Board approval".

It was then moved by Trustee Sanders to amend the Investment Objectives & Guidelines, by adding section 8 as stated by Mr. Fleury, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Report of the Administrative & Accounting Committee:

Committee Chairman Woitkowski stated that due to his absence during the last A&A Committee meeting, he respectively requested that Mr. Fleury report on the meeting held.

Mr. Fleury referred to the draft of Section 7 of the Administrative Rules which have been amended and are up for approval, focusing on Section 7.3.1. He began by explaining that existing references to certain COLA levels being "Pre-funded" had been replaced with the term "assumed". He further explained that the section calls for a Target Rate of Return (TRR) and that the System has never utilized a Target Rate of Return until now. In concert with acceptance of the new rules, a TRR is something which needs to be adopted by the board, so, when adopting the Rule, the board needs to set the initial rate.

In discussions with the Systems actuary and investment advisors, Mr. Fleury explained that an initial TRR of 8% had been recommended. He further noted that the board can amend the TRR at any time and he explained that the current 7.5% earnings assumption will not be effected as a result of adopting a TRR of 8%.

Chairman Pinard asked if the TRR of 8% is not met, how it would affect the COLA decision.

Attorney Rich explained that all the other guidelines would have to be reviewed as part of any COLA consideration. He went on to provide examples of different scenarios under which the trustees might consider the COLA question and noted that in any COLA consideration, the trustee's would review the four COLA guidelines for applicability. He explained that the TRR is present in all four guidelines. The trustees would be comparing the real rate of return against the TRR to determine whether or not any of the four guidelines had been met.

Trustee Porter inquired why the TRR would be different from the earnings assumption of 7.5%.

Trustee Molan commented that the TRR is essentially providing more of a cushion. Trustee Sanders indicated that the TRR would provide the trustees with an additional benchmark of earnings to take into consideration. Committee Chairman Woitkowski noted that when the trustees and actuary reviewed TRR rates from 6% up to 9% and it was determined that the 8% would be the best rate used in the COLA equation.

It was moved by Trustee Molan to adopt the Administrative Rule 7, inclusive of the TRR of 8%, as well as replacing references to "Pre-Funded" with "Assumed", seconded by Trustee Sanders and passed by all those trustees present.

Previous Business:

Indemnification Policy Development Session – Review of progress to date on the development of trustee liability policy - Trustee Sanders commented that Trustee Mercier has been very attentive to the Indemnification Policy and he felt that due to her absence, the matter should be tabled for a future meeting when she is in attendance.

Trustee Porter moved to table the matter, pending full attendance by all the trustees.

Attorney Rich suggested that the board discuss one of the pending issues that do not involve the trustee coverage.

Highlighted on pages one and two of the policy, Attorney Rich pointed out that the indemnification Policy only covers the indemnification of trustees and former trustees. The policy does not cover the staff or the executive director. The statute provides for payment of litigation expenses and payment of liability should any retirement system employees be in that position.

Attorney Rich explained that the NH Retirement System Indemnification Policy was used as a model because the NHRS does not have a statute that covers employees.

Trustee Molan expressed his belief that the Policy should certainly cover the employees. After brief discussion and agreement by the trustees on incorporating language in the policy to cover staff members, Trustee Sanders seconded the motion to table the matter pending full attendance of the trustees and the motion was passed unanimously.

Consent Agenda:

It was moved by Trustee Molan to approve the Consent Agenda, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Other Business:

Trustee Molan asked Mr. Fleury if GASB has adopted the new rules which are expected to have an impact on the valuation.

Mr. Fleury replied yes, however, the rule is not in effect until 2013. Regardless of the required effective date, Mr. Fleury speculated that the nature of the financial statements will change to some extent in 2012 due to the new pronouncements.

Non-Public Session Pursuant to RSA 91-A:3 II(d) For Discussion of Contract Negotiations - Chairman Pinard then entertained a motion to go into Executive Session pursuant to RSA 91-A:3 II(d) at 9:10a.m.(Consideration of the acquisition, sale, or lease of real or personal property which, if discussed in public, would likely benefit a party or parties whose interests are adverse to those of the general community.)

Roll Call Vote:

Ayes: Messrs. Sanders, Woitkowski, Pinard, Porter, Molan

Nays: None

Following the conclusion of the Non-Public Session, Chairman Pinard then entertained a motion to seal the minutes of executive session pursuant to RSA 9-A:3 III.

Trustee Molan moved to seal the minutes of executive session, seconded by Trustee Porter and passed unanimously by all those trustees present.

Trustee Molan then requested that Mr. Fleury provide a preview of agenda items scheduled to be addressed at the August, Board of Trustees meeting.

Mr. Fleury reported that the August Board of Trustees meeting will include reports from the MECRS actuary and investment advisor. The investment advisor will present an asset allocation plan and the actuary will report on the results of the 5-year experience study, for the board's consideration.

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 9:27 a.m., seconded by Trustee Sanders, and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard E. Fleury
Executive Director