

August 13, 2013
Minutes #494

Minutes of the Board of Trustees' Meeting -1-

Call to Order: Acting Chairman Molan called the meeting to order at 8:42 a.m.

Present: Trustees: Richard Molan, Robert Lynch and Mike Woitkowski, Bill Sanders and Dianne Mercier (Trustee Mercier departed at 9:50 a.m.)
MECRS Staff: Gerard Fleury, Sandi Aboshar and Suzanne Wilson

Absent: Chairman Donald Pinard & Mayor Gatsas

In Attendance: Attorney John Rich of the McLane Law Firm and Kevin Leonard of New England Pension Consultants

Approval of the Minutes of the Previous Board Meeting:

Due to the absence of Chairman Pinard, Trustee Molan agreed to serve as Acting Chairman for the meeting. Acting Chairman Molan entertained a motion to approve the minutes of the previous meeting. Trustee Lynch moved to approve the board minutes of July 9, 2013, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Approval of the Immediate Meeting Agenda:

It was then moved by Trustee Woitkowski to approve the immediate meeting agenda, seconded by Trustee Lynch, and passed unanimously by all those trustees present.

Report of the Executive Director:

Status of MECRS CAFR for 2012: Mr. Fleury began by informing the board that the MECRS Comprehensive Annual Financial Report had been printed and mailed to plan participants in addition to being posted on the MECRS web site.

Closure of Vestigial Remains of CIGNA Portfolio: Next, Mr. Fleury reported that the MECRS has carried the illiquid remains of a real estate investment with CIGNA, valued at only a few thousand dollars, for several years. He noted that the System is now in receipt of a notice that the final distribution will be wired to the MECRS cash account at State Street Bank at the end of September.

Reporting & Budget Implications of GASB 67 & 68: Mr. Fleury informed the trustees that he had scheduled, Mr. Ken Alberts of Gabriel, Roeder, Smith & Company, to be present at the September 10, 2013 Board of Trustees meeting to discuss the implications of GASB 67 & 68 on the financial reports of the City and the pension fund. Whereas the question of cost absorption and a potential doubling of actuarial expenses will be involved, Mr. Fleury noted that trustees are asked to make every effort to attend this important session.

August 13, 2013
Minutes #494

Minutes of the Board of Trustees' Meeting -2-

Report on Operational Difficulties With the Custodian Bank: In recent months Mr. Fleury reported that the System had been engaged in rebalancing its investment portfolio in line with recommendations put forth by the System's investment advisor and approved by the board. While all of those directives were successfully completed he stated, there had been an unnecessary degree of uncertainty associated with several transactions. He indicated that the primary cause of staff concerns stem from the lax responsiveness of the System's custodian and the inadequacy of reporting tools provided by the custodian for time sensitive transactions.

After brief discussion on the matter, Trustee Sanders suggested that Mr. Fleury contact the Chairman of State Street Bank for assistance in resolving his dissatisfaction with the custodial services.

Report of Public Employee Retirement Summit: Mr. Fleury reported on his recent attendance at the 2013 Public Funds Summit in Newport, RI from July 22nd to July 24th. He informed the board that the summit focused on the favored use of fixed income as a defense against market volatility and also on the lingering public criticism of DB plans. Other topics included class actions associated with shareholder rights, risk management, trustee education, asset allocation models, and alternative asset strategies. Mr. Fleury noted that further details on the seminar are available on the Internet and that he felt that the summit provided valuable insight on trends and events in the public funds universe.

Report of the Benefits Committee:

Committee Chairman Lynch reported that the Benefits Committee Meeting had met earlier in the morning to discuss the committee's review and recommendation to proceed with an amendment to Chapter 218 regarding the Defense of Marriage Act (DOMA) and a change to the minimum participation standard relating to the School District. In addition, he reported on the status of a member's request on the voluntary renunciation by a named beneficiary of a retiree. He informed the trustees of the Benefits Committees recommendation, not to move forward with that particular proposed legislative change.

Acting Chairman Molan expressed his appreciation for the thorough review conducted by legal counsel regarding the renunciation of benefits by a named beneficiary and he described legal counsel's recommendation in greater detail. In summary, was not to proceed with the requested legislation as it was not permitted under Tax Code regulations and as a result could jeopardize the qualified status of the Plan He then entertained a motion to deny the request from a member seeking that legislative change.

Trustee Sanders moved to deny the request regarding the volunteer renunciation of a retiree's named beneficiary, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Minutes of the Board of Trustees' Meeting -3-

It was then moved by Trustee Woitkowski to authorize Mr. Fleury to proceed with the DRAFT amendment to Chapter 218 for DOMA and minimum participation in accordance with the recommendations of the Benefits Committee, and to begin seeking sponsors for the legislation, seconded by Trustee Sanders and passed by all those trustees present.

Consent Agenda:

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

New Business:

Trustee Fiduciary Education - NEPC representative was present to conduct an educational session on Private Equity Investment Opportunities including the prospects for a bank loan component and to discuss minor amendments to the Investment Guidelines in recognition of a benchmark change for Wellington Capital

First, Mr. Kevin Leonard of New England Pension Consultants notified the trustees of NEPC's office relocation to 255 State Street, Boston, MA in September. As a prelude to next month's formal June 30th investment performance review, Mr. Leonard stated that preliminary numbers have the overall portfolio up 11.7%.

Mr. Leonard then provided the trustees with a brief summary of the Weekly Markets & Indicators for week ending August 9, 2013, noting good performance by equities and emerging markets asset classes though somewhat volatile.

Mr. Leonard summarized NEPC's recommendation regarding the amendment to the Investment Guidelines in recognition of a benchmark enhancement for Wellington Capital. He reminded the board that Wellington's Diversified Inflation Hedges strategy is to provide exposure to inflation sensitive assets in order to capture the effects of inflation (beta). The portfolio is designed to respond when inflation is high, while protecting on the downside when inflationary pressures are not present in the market environment

The purpose for the benchmark change, Mr. Leonard stated, is to allow Wellington to employ a static passive benchmark that will not change, in order to better measure the value added from capital allocation. As such, Wellington plans to use the new benchmark going forward, which consists of 50% MSCI ACW Commodity Producers Index (energy, metals and agriculture), 25% commodities Dow Jones UBS Index and 25% Barclays US Tips Index.

Having reviewed the new benchmark with Wellington and internally, Mr. Leonard stated that NEPC finds the new benchmark consistent with Wellington's strategy, and is recommending the MECRS utilize the new benchmark for the Wellington Diversified Hedges product.

Minutes of the Board of Trustees' Meeting -4-

Amendment to Wellington Capital Benchmark: Referring to New Business Item #4, it was moved by Trustee Sanders to approve NEPC's recommendation as stated, to amend the benchmark for Wellington Capital, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Moving on, Mr. Leonard referred to a past meeting with MECRS Investment Committee, where NEPC representatives presented the committee with a private equity strategic plan, which is a budget for what the board should spend on any year within the private equity portfolio. Currently, MECRS has a target of 5% to private equity and over the long term Mr. Leonard stated, NEPC would like the portfolio to be well diversified, not only by private equity type, but also by vintage year, by not putting all the funds to work in one year. He explained that each year MECRS will be given a projection on how much money the board should consider investing in any vintage year.

Mr. Leonard informed the board that two options were presented to the Investment Committee. The first option was to allocate \$5 million to a fund of funds private equity manager for vintage year 2013 which was a firm wide recommendation. Option 2, Mr. Leonard continued, is a split allocation of \$3 million to fund of funds and a \$2 million allocation to direct lending. To elaborate further on that option, Mr. Leonard referred to a booklet distributed at the start of the meeting entitled, Direct Lending Overview.

Referring to page 39 of the booklet, Mr. Leonard summarized the list of recommended direct lending managers and their fund description. He noted that the appeal of direct lending is that MECRS would be lending money and receiving a quarterly income payment including a quarterly interest charge. From a duration standpoint, the life of a fund typically falls within a 5 to 6 year cycle.

Mr. Leonard explained the difference between the US products and European opportunities noting that the US Managers have more regulatory oversight than the European Managers, whereas the European Managers have a higher rate of return, with more risk. He noted that most NEPC clients are looking at both US and European companies to complement each other, however, NEPC is recommending that MECRS contemplate only a US company as a starting point.

Trustee Sanders referred to the private equity historical record of successes and failures and he asked Mr. Leonard, why the opportunity of the private debt arena is just now being introduced to clients.

Mr. Leonard replied that the direct lending opportunity is an extension of the opportunity in fixed income, tradable bank loans, high yield and investment grade credit and also part of Fund of Funds. Mr. Leonard explained that as a result, the direct lending opportunity would lower the future return of the private equity portfolio. The current allocation of 5% in private equity was

Minutes of the Board of Trustees' Meeting -5-

based on a long term return of 13% to 15%. Direct Lending would lower the return, with a shorter duration, with less risk and provide a quarterly income, therefore, supplying the needed liquidity.

Mr. Fleury asked Mr. Leonard, to describe the market for direct lending and if there is a time constraint as to when MECRS should consider adopting the opportunity. Mr. Leonard responded that if the board is interested in the direct lending asset class, he recommended that the trustees should schedule the interview of the suggested fund managers in September.

Trustee Mercier expressed her concern regarding the proposed opportunity due to the risks associated with lending to lower-mid market companies.

Mr. Leonard stated that NEPC believes that it is worth MECRS Investment Committee's time to do further due diligence on the asset class by having interviews with the Direct Lending Managers for a question and answer session. This would be only for the purpose of possible consideration of adding the asset class, with no obligation to hire a manager.

After brief discussion, the trustees agreed to schedule and Investment Committee Meeting and to conduct interviews of the suggested managers within the next 30 days.

Mr. Leonard suggested that he first contact the NEPC approved managers for their availability and time constraints and that he would then work through Mr. Fleury to determine a meeting date and schedule the managers.

Summary Recommendation – Application for Disability from Thomas Moran – Mr. Fleury reported that Mr. Moran had met all the requirements for disability and he stated that it was his recommendation that the board approve the disability request.

It was moved by Trustee Sanders to approve the disability application for Mr. Moran, seconded by Trustee Lynch and passed unanimously by all those trustees present.

Request for Motion – Annual Report on Gainful Occupation – Mr. Fleury referred to the summary of gainful occupation for 2012, included in the trustee's agenda packets and requested that the board move to accept and place the report on file.

Trustee Lynch moved to accept the 2012 Gainful Occupation Summary, seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Allocation of Excess Cash – Mr. Fleury referred to the new Consent Item #10 included in the trustees packets, which details cash flow for the organization. Pursuant to the cash flow policy adopted by the board at the June 2013 meeting, Mr. Fleury stated that the report indicates the existence of cash balances above the target level, which the board may wish to invest in the newly established S&P 500 Index Fund, to await capital calls. Mr. Fleury went on to explain

Minutes of the Board of Trustees' Meeting -6-

that the MECRS portfolio tends to be overweight in cash and the board is making commitments to various purposes, that don't require immediate funding. The design of the S&P Index Fund will allow the System to park excess cash until such time as it is needed, with the understanding that when a capital call is due, administrative staff would have the authority, based on motions made in prior public sessions, to withdraw the money from the Fund to meet the capital call requirements.

Consent Agenda Item #10 tracks the transfers of the S&P 500 Index Fund and provides the trustees with reconciliation of those transactions.

Mr. Fleury informed the trustees that the new Monthly Cash Management Report indicates that the System currently has a little over \$3 million cash in excess of their target allocation.

It was moved by Trustee Sanders to allocate \$3 million into the S&P 500 Index Fund with the caveat that the Executive Director be empowered to withdraw those funds in order to meet capital calls should they materialize on short notice, seconded by Trustee Woitkowski and passed by all those trustees present.

Other Business:

Acting Chairman Molan moved to recess the meeting at 10:00 a.m.

Acting Chairman Molan reconvened from recess at 10:10 a.m.

Acting Chairman Molan then entertained a motion to approve the terms of the settlement term sheet dated July 24, 2013 between Chairman Donald Pinard on behalf of the MECRS and Regions Bank. Trustee Sanders moved to authorize Chairman Pinard to execute the formal settlement agreement required by the settlement term sheet with Regions Bank, seconded by Trustee Lynch and passed by all those trustees present.

Motion to Adjourn:

Having completed all of the items of business for the day, Acting Chairman Molan and entertained a motion to adjourn. Trustee Lynch moved to adjourn at 10:11, seconded by Trustee Woitkowski, and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard Fleury
Executive Director

