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Minutes #533

Minutes of the Board of Trustees' Meeting -1-

- Call to Order:** Acting Chairman Sanders called the meeting to order at 8:30 a.m.
- Present:** Trustees: Bill Sanders, Dick Molan, Mike Woitkowski, Bob Lynch and Dianne Mercier
MECRS Staff: Gerard Fleury and Sandi Aboshar
- Absent:** Mayor Gatsas
- Excused:** Donald Pinard
- In Attendance:** Attorney John Rich, from McLane Middleton, Professional Association and Kevin Leonard, Sebastian Grzejka, both from NEPC

Approval of the Minutes of the Public Hearing held February 21, 2017:

Due to the excused absence of Chairman Pinard, Trustee Sanders agreed to serve as Acting Chairman for the meeting. Acting Chairman Sanders entertained a motion to approve the minutes of the Public Hearing held February 21, 2017. Trustee Woitkowski provided that motion which was seconded by Trustee Molan and passed unanimously by all those trustees present.

Approval of the Minutes of the Previous Board Meeting:

Trustee Woitkowski moved to approve the minutes for the board meeting held February 21, 2017. Trustee Lynch seconded the motion and it was passed unanimously by all those trustees present.

Approval of the Immediate Meeting Agenda:

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

Report of the Executive Director:

New IRS Determination Letter Received: Mr. Fleury was pleased to report that on February 21, 2017, the IRS issued a Favorable Determination Letter to MECRS, to replace the original, issued back in 1975 and that copies have been shared with the MECRS auditors.

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2016 Inflation and 2017 COLA Computations are Ready for A&A Committee Review: Moving on, Mr. Fleury stated that the United States Department of Labor has issued inflation figures for calendar year 2016. In addition, the information required to perform a COLA Affordability Calculation will officially be in hand, should the Board accept the Actuarial Valuation later in this meeting. Mr. Fleury noted that the A&A Committee may want to schedule a meeting to review CPI results and the results on the Cola Affordability Calculation, pursuant to Administrative Rule 7, and to formulate a recommendation for the full Board's subsequent action.

Employee Recognition: Next, Mr. Fleury recognized, Ms. Aboshar, Executive Assistant, for one of the many things she does to make MECRS member client service, all that it can be. Mr. Fleury elaborated on a situation facing a retiree, and residing in a South American country. Because direct deposit does not exist in the country, retiree payments must be made by check, and the mail service in South America is inefficient. The retiree, obtained the services of an advocate because his payments were not being received and the Retirement System's records confirmed that checks were going un-cashed. Ms. Aboshar was able to work with State Street Bank to stop payment on the missing checks and arrange for them to be reissued. Normally, this is not a difficult task, but communicating with the foreign country had its challenges. A complimentary message was received from the advocate, which confirmed that Ms. Aboshar's actions had been effective and that all the retiree's payments were now accounted for.

Status of RFP for Custodian Bank: For some months, Mr. Fleury has reported his frustration with the quality and responsiveness of custodial services provided by State Street Bank & Trust. He stated that after a number of telephone conferences with representatives at State Street Bank, the System is finally seeing positive results. Instruction and assistance with cash flow tools have been received and availability of reports needed to run the System's operations, have improved dramatically. Nevertheless, Mr. Fleury noted, this fresh new interest in providing the System with the level of service required, may be associated with the recent assignment of new representatives to the MECRS account. Frequent unannounced representative changes was one of the complaints with State Street Bank, and only time will tell whether this problem has truly been addressed. Mr. Fleury explained his ongoing concern, that the sudden assignment of other representatives may result in a return to the poor service and frustrations of the past. Mr. Fleury stated that he continues to work on a draft RFP, designed to provide the System with an opportunity to change banks, if so desired. The draft RFP will not incur costs or obligation to the Retirement System, however, moving forward, Mr. Fleury requested permission from the board to proceed with its issuance of the RFP and report on its progress in the coming months. The trustees were in agreement and granted permission for Mr. Fleury to move forward with the draft RFP.

Final Training Received on MECRS Website: Next, Mr. Fleury stated that after receiving instructions on the final and most complicated segment of the MECRS website, the

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administrative staff is now able to update all of the content on the new website without the need for assistance from the site developer.

IME Difficulties: Mr. Fleury informed the trustees that it has become difficult to find physicians, to conduct Independent Medical Exam's for members' requesting a disability benefit and also that IMEs have grown in cost, compared with historical norms. If this current trend continues, Mr. Fleury stated, it may become necessary to send disability applicants to neighboring States for their exams. Local physicians are no longer interested in performing exams or are charging 4 to 5 times what the System was charged in the past.

Meetings with Crescent & Pzena: Mr. Fleury reported that he had met with Mike Rogers of Crescent Direct Lending on March 20th to review the investment process with Crescent, and to hear about their future plans. In summary, Mr. Fleury explained, Crescent's fund is beginning to unwind and they are looking for investors for their next offering. Mr. Rogers was directed to contact NEPC since they would determine the applicability and timing of any future interest the System may have. Mr. Fleury reported that on March 21st, he had met with Wayne Palladino and Benjamin Silver of Pzena Investment Management, to review the portfolio's performance. Mr. Fleury concluded that Pzena seems mildly optimistic of future results and has expressed interest in managing money in sectors other than large cap. Mr. Fleury directed their interest to NEPC.

Member Informational Session Conducted at Water Treatment Plant: On March 23rd, Mr. Fleury conducted a requested informational session at the Water Treatment Plant for members of the System. The session focused on the Additional Contribution Program and of the six people in attendance, two immediately elected to participate in the program and paid for the cost of their initial calculation.

Participation in 2017 Opal Public Retirement System Summit: In closing his report, Mr. Fleury informed the board of his scheduled participation in the 2017 Opal Public Employees Retirement Summit in Newport, RI on July 24, 25 & 26. Mr. Fleury stated that he has been invited to participate on a roundtable panel, to discuss events impacting public plans. Mr. Fleury stated that due to his willingness to participate in the roundtable forum, the cost of attending the summit will be absorbed by Opal Public Retirement.

March Consent Agenda:

Trustee Molan moved to approve the March Consent Agenda, seconded by Trustee Lynch and passed unanimously by all those trustees present.

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April Consent Agenda:

Trustee Molan moved to approve the April Consent Agenda, seconded by Trustee Lynch and passed unanimously by all those trustees present.

New Business:

Acceptance of the 2016 Preliminary Actuarial Valuation Discussed Informally on March 14, 2017 - Mr. Fleury placed a conference call to Mr. Ken Alberts of Gabriel, Roeder, Smith & Co, to answer any questions with respect to the 2016 Actuarial Valuation.

First, Mr. Fleury stated that owing to the lack of quorum, for the MECRS Board Meeting, scheduled for March 14, 2017, the trustees held an informal session and had the opportunity to review the preliminary 2016 Actuarial Valuation.

Acting Chairman Sanders stated that he was not in attendance during the valuation presentation held on March 14, 2017, but that he has had the opportunity to review the preliminary valuation. He noted that the valuation resulted in an increase in the employer contribution rate from 23.74% to 24.45%, as well as the true-up credit amount of \$146,479.00, for a six month period. Acting Chairman Sanders explained that the true-up is to account for the differences in actual and assumed payroll that would have affected the contribution, had the City been making contributions on a payroll period basis.

Acting Chairman Sanders asked Mr. Alberts if there were any other issues in the preliminary valuation that he wished to discuss with the trustees. Mr. Alberts asked the board to turn to page A4, to review the future outlook of the Plan.

Mr. Alberts explained that funding value of assets recognizes assumed investment income fully, each year. Differences between actual and assumed investment income are phased-in over a closed 5-year period. During periods when investment performance exceeds the assumed rate, funding value of assets will tend to be less than market value. During periods when investment performance is less than the assumed rate, funding value of assets will tend to be greater than market value. The Development of Funding Value of Assets chart indicates that there will likely be upward pressure on future contributions moving forward, resulting in future contribution increases in the coming years.

Pending the completion of the 5-year experience study, Mr. Fleury stated that the results of that study may have an impact on rates for 2018, which Mr. Alberts confirmed to be correct.

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Attorney John Rich of the McLane, Middleton Law Firm asked Mr. Alberts to elaborate on the comment made on page A-7 of the preliminary valuation, which states that the employer contribution rate derived in the valuation does not guarantee benefit security.

Mr. Alberts responded that the point of the statement is to remind and encourage the board of the implied Funding Policy and that the trustees consider benefit security, when they are adopting a contribution rate each and every year.

Acting Chairman Sanders stated that the MECRS Board has relied on GRS to set the contribution rate that is reasonable for the City as well as adjusting the assumed rate of return. Based on the preliminary actuarial report presented, Acting Chairman Sanders further stated that the board has not identified any factors regarding the contribution rate, which they find to be relevant at this time that would suggest a different contribution rate is required.

Trustee Molan moved to accept the 2016 actuarial valuation presented and place it on file, seconded by Trustee Lynch and passed by all those trustees present.

Mr. Fleury then noted that the Funding Policy is currently informal, but that he has drafted a formal written Funding Policy for review by the Administrative & Accounting Committee, followed by formal adoption by the full MECRS Board.

There being no further need to continue the telephone link with Mr. Alberts, Mr. Fleury thanked him for his time and expertise and ended the conference call.

Approval of the Liquidity and Cash Management Policy - Mr. Kevin Leonard and Sebastian Grzejka were present to discuss cash flow requirements and to discuss minor changes that have been made to the Investment Policy.

Mr. Fleury directed the trustees attention to the Liquidity and Cash Management Policy, included in their agenda packets. He explained that the policy recognizes that some longer term objectives include routine periodic capital calls on investment commitments, and the collection of distributions and redemptions which, by their nature, are paid out over time and not at specific dates. He explained that because the Board contracts with an investment consultant to recommend investment allocations, and depends upon administrative staff to carry out the objectives approved by the trustees, a need exists for a policy which authorizes administrative staff to execute the directives of the board.

Mr. Fleury indicated that the policy also requires that the board be informed on a monthly basis, of the cash balances held by the System. He noted that under the proposed policy, the

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monthly report will identify projected receipts and disbursements for the upcoming quarter in as accurate a manner as possible, given the uncertainty of capital calls and distributions from asset classes such as private equity. The monthly cash management report will be compiled by the Executive Director, who shall also sign the report. The report will then be included on the Consent Agenda of each monthly board meeting, where its acceptance by the Trustees will acknowledge their oversight of the delegated cash management practices.

After lengthy discussion on the unforeseen timing of liquidations, within the parameters of the MECRS Draft Liquidity & Cash Management policy, Mr. Grzejka, turned the trustees' attention to page 2 of the Rebalancing Recommendation Booklet and outlined NEPCs' recommendations to maintain cash for investment and operating needs.

Mr. Grzejka stated that NEPC recommends the Board approve the DRAFT policy and if funds are needed in between meetings, the policy would allow the Executive Director to raise funds with a recommendation from the Investment Advisor from across the portfolio. NEPC also recommends maintaining cash at target with regular rebalancing to maintain this level of cash.

Mr. Grzejka stated, the final piece of the rebalancing recommendation is to provide incremental cash. In order to accomplish that goal, NEPC recommends that the board approve distributing interest and dividends, where possible, instead of reinvesting such income.

Acting Chairman Sanders stated that he is uncomfortable with the DRAFT policy as presented.

The Executive Director informed the trustees that some form of liquidity policy will be needed eventually so as to be able to access cash for capital calls in between meetings. He has spent time working with State Street Bank & Trust to determine, on a daily basis, the MECRS's cash account balance in order to refine cash flow needs.

Attorney Rich referred to the cash management report included in the agenda packet and asked Mr. Fleury whether the investment distributions, cash inflows and outflows, are monthly or quarterly, to which Mr. Fleury responded that the distributions are determined by the managers. Depending upon the asset class, some are monthly; however for real estate investments in particular, the actions are quarterly.

Trustee Mercier suggested that the policy require consultation with the MECRS Board Chairman or the Investment Committee Chairman. She also suggested that these officials could be designated in the event that the Executive Director was not available.

Based on the trustees suggestions and after reviewing other options within the funding policy, Mr. Fleury stated he would develop a revised DRAFT, Liquidity and Cash Management policy for the boards' review and it could be presented at a subsequent meeting.

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Trustee Molan moved to table the approval of the Liquidity and Cash Management Policy, seconded by Trustee Lynch and passed unanimously by all those trustees present.

Moving on, Mr. Grzejka, referred to page one of the rebalancing recommendation, bringing the MECRS portfolio closer to target. He stated that NEPC believes in seeking to add value at every step in the investment management process and that it is critical for plan sponsors to focus resources on the highest value-added components of the investment management process.

Mr. Leonard stated that the rebalancing recommendation looks to accomplish three goals. 1.) To complete reallocation of international equity mandate and bring it to target, 2.) Adjust active passive weighting of the large cap allocation. 3) Bring cash to target to help offset cash needs for the portfolio.

Mr. Leonard explained that active management is more likely to add value in less efficient areas of the capital markets and is less likely to add significant value in more efficient areas of the capital markets. NEPC recommends maintaining a blend of active and passive strategies, however, there is potential to resize the exposures in the future.

Based on the rebalancing recommendation to transfer \$10.5 million between various accounts, Trustee Molan made a motion to accept NEPC's recommendation and to transfer \$2,000,000 from Mellon Capital, \$500,000 from PIMCO, \$4,000,000 from Pzena, \$2,000,000 from Sands Large Growth, and \$2,000,000 from Rothschild Small Cap, and to invest \$4,000,000 into Vanguard, \$4,500,000 into Gryphon and \$2,000,000 into the S&P cash account. Trustee Woitkowski seconded the motion, the vote was taken, and the motion carried by all those trustees present.

Trustee Molan stated that he would like to schedule an Investment Committee meeting after the May Board meeting to continue discussion regarding the rebalancing of the MECRS portfolio. Mr. Fleury replied, he would see to the details.

Lastly, Mr. Grzejka referred to the presentation booklet, Investment Summary, as of February 28, 2017 noting the total composite of the MECRS's portfolio, market value of \$209,940,213. He provided details of each manager within the portfolio and reported it has been a great start to 2017.

In terms of the asset allocation moving forward, Mr. Grzejka stated, private equity will be the priority along with the continued active, passive discussion.

Lastly, Mr. Leonard stated that NEPC was monitoring the merger of Standard Life and Aberdeen Asset Management which was recently announced.

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Motion to Adjourn:

Having conducted all the business of the day, Trustee Molan moved to adjourn the meeting at 9:47 a.m., seconded by Trustee Woitkowski and passed unanimously by all those trustees present.

Respectfully Submitted,

Gerard E. Fleury
Executive Director