Town of Palm Beach Retirement System
Board of Trustees
Minutes of November 18, 2016 Meeting

I. Call to Order and Roll Call

Chairman Ross called the meeting to order at 9:00 am in the Town of Palm Beach Hall Chambers, 360 South County Road, Palm Beach, Florida 33480

In Attendance:

TRUSTEES:
Wilbur L. Ross, Chairman
Brett Madison, Secretary
Tom Bradford, Town Manager
Daniel Stanton
Bradford Kaufman
Jeffrey Amling
Michael Marx

ALSO PRESENT:
William P. Hanes, Retirement Administrator
Jane Struder, Finance Director
David West, The Bogdahn Group
Dan Johnson, The Bogdahn Group
Danielle Olson, Human Resources Director
Pete Strong, GRS
James Linn, Attorney

Gerald Goldsmith joined the meeting at 9:06 a.m.

Absent:
Dan Wilkinson

II. Approval of Agenda

Mr. Bradford made the motion to approve the agenda. Mr. Stanton seconded the motion. The trustees unanimously approved the agenda.

III. Comments by Trustees

Mr. Marx announced that he is on duty and his speakers will be on in case that he is needed. Mr. Hanes commented that Officer Wilkinson notified him earlier in the morning that he had been involved with a Police matter, and would not be able to attend the board meeting.

IV. Public Comments

None

V. Approval of Minutes: August 19, 2016

Mr. Stanton made the motion to approve the minutes of August 19, 2016. Mr. Ross seconded the motion. The trustees unanimously approved the motion.

VI. Financial Report and Disbursements, Jane Struder, Finance Director

Ms. Struder presented the quarterly financial report. She noted that the Town does not need to transfer money from the money managers this quarter. Ms. Struder presented the disbursement report from August 1st through October 21st.

The trustees accepted the report without motion.

VII. Investment Report, Dave West and Dan Johnson

A. Quarterly/Annual Investment Performance Report

Mr. West discussed some administrative updates with the Board. He discussed the letter from the president and CEO of The Bogdahn Group announcing the rebranding of the firm. He discussed their commitments and that there was going to be a name change, but he could not disclose the new name of the group at the time. He commented that the name change has no impact on the operation. Mr. Stanton asked if there is a story behind the story, for the new changes. Mr. West stated that the story is that the firm wants to make sure that they have a good succession plan in place because of their rapid growth, and will be bringing in competent people. Mr. Stanton asked about Mr. Bogdahn. Mr. West stated that Joe Bogdahn has moved on to other endeavors.

Mr. Ross asked if Joe Bogdahn has retired. Mr. West stated that Mr. Boddahn has retired from the financial industry, but is starting new businesses. Mr. Johnson stated that The Bogdahn Group will remain an employee owned firm and that the only difference will be a name change. He stated that the story behind the story is a marketing strategy for the organization, but everything else will remain exactly the same.

Mr. Kaufman stated the Board wants to make sure there is no legal changes going on that can distract the firm from its objectives. Mr. Ross requested if over the next few meetings there are other personnel changes in the firm that Bogdahn let the Retirement Board know.

Mr. West reviewed the Quarterly Investment report, and stated the good news of a good return for the fiscal year. He provided an overview of the investment performance, including financial market conditions, Domestic Equity, International Equity, Fixed Income, Alternatives, Hedge Funds, Commodities, Private Equity, Real Estate, and discussed the manager roster.

Mr. West reviewed the summary of events. Mr. Hanes asked Mr. West to express the performance at "net of fees." Mr. Stanton commented about how active managers are being beat by the index funds and that The Bogdahn Group at some point should address it. He discussed how the Town Hedge Funds are doing terrible and commented that not all Hedge Funds are performing bad. Mr. West answered that they (Bogdahn) will add it to their agenda item for future discussion. Mr. Stanton stated that he is not advocating for Funds, but feels that is a topic that needs to be discussed. Mr. Goldsmith suggested that Bogdahn add the active fees paid as an additional item for future discussion. Mr. West stated they would make sure to add it to a focus discussion. Mr. Goldsmith commented that he would be asking about cash flow during the meeting.

Mr. West reviewed high points on various asset classes on reported returns. Mr. Kauffman asked if performance based fees are backward looking and if there is a look back period. Mr. West answered that there is no look back period for fee arrangement. Mr. Stanton asked for clarification purposes if TSW small cap value is in the bottom of their group. Mr. West answered Mr. Stanton is correct, and TSW small cap value is in the bottom of the group for that particular year. Mr. West stated that TSW mid cap value fund and the TSW small cap have been merged into the SMID cap product, which is a different product that will be dropping off. Mr. Stanton commented that it seems like what they did was sweep the product that was doing really bad into the one that was doing okay to end up with something reasonably acceptable. Mr. West answered that the changes will bring better efficiencies from a return standpoint as well as from fees standpoint. He stated that Mr. Stanton's observations are one hundred percent accurate.

Mr. West summarized International performance was a good performance. He commented that Emerging Markets were up above the benchmarks. He stated that fixed income was above the benchmarks over the period. He commented that the alternative assets were a net below benchmarks. He discussed that the REIT stocks were up 19.6%, but commented that REITs are overvalued and Bogdahn recommends that the plan move completely out of REIT equities.

He discussed Private Equity allocation, and summarized the full schedule of private equity and private equity real estate investments with drawdowns and distributions. He discussed the annual cash flow and the movement of funds, including activities in contributions, distributions, management fees administrative fees, investment earnings and appreciation, and concluded there is a net result of $15 million to help retire cash flow.

Mr. Hanes asked Mr. West to discuss the long-term view of cash flow and investment from 2012 to 2015, which resulted in a net cash flow reduction of over $41 million. Mr. Goldsmith commented that he just wants to make sure that the Town has enough cash to pay the bills. Mr. West stated that they would be working very closely with GRS to insure that the investments are aligned properly with the cash flows as well as the target rate of return requirements.

Mr. Goldsmith commented that if the world is reporting that pension funds are not making more than 2% or 3%, then why is the board presenting that it is making 7% or 8%? Mr. West stated that there is a bit of misrepresentation by the reporting community, and that this has been a significant period of mending and that it depends on the source reporting. He commented that this has been a good period for mending for most plans. Mr. Goldsmith noted that he just wants to make sure that the statistics are truthful. Mr. Linn noted that most plans performed much worse as of June 30, but he imagined the September 30 performance was good. Mr. West stated that the current June 30 to June 30 period was one of the worst. He referenced the public fund database, and stated that the plan median return for the year was 9.42%. Mr. Hanes stated that the S&P 500 index for the same fiscal year period was over 15%. Mr. West agreed. Mr. Amling asked if any changes will be made in the Private Equity mix or does the liquidity exit provision state that it cannot be done? Mr. West answered yes, and the Private Equity provision will be kept in the future.

Mr. Stanton asked Mr. West what is the time frame on rearranging the Non- US Equity class where the Town is heavy and underweighted in Domestic Equity. Mr. West answered that if the Board approves the Investment Policy Statement today, which addresses the asset allocation issue, that they have put together a list of items that they want to execute after today's meeting that will place them with their new target. Mr. Hanes asked Mr. Linn if the Town Council has to adopt the resolution before implementation. Mr. Linn answered that the changes to the investment policy statement is subject to the approval of the Town Council. Mr. West stated that they are making some significant changes to the allocations and changing the boundaries as currently permitted in the Investment Policy Statement. Mr. Linn stated that if the Retirement Board approves the recommendation, after he reviews them, if they meet the state requirements, then it is up to the Town Council to put their stamp of approval before they can be executed.

B. Investment Policy Statement (IPS) Restatement

Mr. West reviewed the Investment Policy Statement (IPS). Mr. Kaufman suggested that it is best to have the summary of change next to the actual document, so the board can see the changes. Mr. West reviewed the target allocations, investment performance objectives and investment guidelines. Mr. Ross asked if the changes in the defined benefit plan for the police made by Town Council are reflected in the mix. Mr. West answered yes, that these changes recommended reflect the investment of the define benefit asset pool. Mr. Ross asked how much margin there is for error over the actuary necessity. Mr. West answered that their forecast is probability based and puts them in reasonable operating parameters. Mr. Ross asked how much above 7% is the Bogdahn Group strategy based on their model. Mr. West stated that their target return with this system is about 7.3% or 7.5%. Mr. Johnson stated that it is based on the asset allocation review from the last meeting, when that document was revised, and the expected rate of return is around 7.6% with a standard deviation within one year of 11.7%. Mr. Ross asked why 7.6% is the target if the Town is trying to achieve 7.4, 7.3, 7.2, and 7.1 in consecutive years. Mr. Johnson answered that this is just clarifying what was reviewed in the last Board meeting. Mr. Johnson clarified that this document replaces the prior document and is in line with the state guidelines. Mr. Bradford asked if there are any changes to the criteria for the investment manager review. Mr. West stated that this is a complete re-write doctrine, and there were more items added to the list and some of the information was pulled from their operating manual.

Mr. Goldsmith made the motion to approve the Investment Policy Statement. Mr. Kaufman seconded the motion. The trustees unanimously approved the motion.

Mr. Stanton asked if they have people looking for Hedge Fund managers that are outperforming. Mr. West answered that they have staff specialists researching and looking for the better performing funds. Mr. Ross asked if there are any funds that they are recommending currently. Mr. West answered yes, and they would like to emphasize the Hedge Funds later in the cycle. Mr. Ross asked if the Town is not in the later stage right now. Mr. West answered that there is fiscal policy and monetary policy that needs to be implemented.

C. Real Estate Interviews

i. Morgan Stanley, Meg Golder

Meg Golder was the presenter for Morgan Stanley. Mr. Kauffman disclosed that he has a professional relationship with Morgan Stanley. Mr. Ross asked about the interest rate environment. Ms. Golder answered that Morgan Stanley only had five years of negative performance, and in the CBD market they expect markets to hold better and increasing interest rate has not affected it. Mr. Ross commented that we are in unprecedented low rates now and does not understand why there is no growth. Ms. Golder answered that their annual growth over the last five years is about 7% and that they are 95% leased. Mr. Bradford asked if they want to go industrial. Ms. Golder answered that 80% of their acquisitions are industrial. Mr. Bradford asked if warehousing is industrial. Ms. Golder stated yes and that is the majority of what they own within their industrial space. Mr. Kauffman asked how much cash is Morgan Stanley sitting on. Ms. Golder stated about 1.5% of the $17 billion. Mr. Johnson asked how long comes in the quarter. Ms. Golder answered that about two or three quarters and they are reinvesting in their current properties. Mr. Stanton asked who are their two or three biggest competitors and what do they do better. Ms. Golder answered that one of their biggest competitor is JPMorgan. Mr. Stanton asked if there is anything that Morgan Stanley wishes they did like their competitor. Ms. Golder answered that they would like to improve their performance in industrial. Mr. Johnson asked what is the projected income for next year. Ms. Golder answered that their income in the last several years has been about 4.5% and their return has been averaging 15%. Mr. Ross asked what has been the latest cash flow rate of return. Ms. Golder answered the dividend return is 4% and the income of 4.4% for the last year. Mr. Johnson asked to explain the administrative calculation of their fees. Ms. Golder answered by reviewing the fee structure from the Morgan Stanley presentation. Mr. Goldsmith asked if the cash return is after fees. Ms. Golder answered the dividend is after fees.

ii. JP Morgan, Kate Morgenier Alexia Gottschalch and Jennifer Ciullo

Ms. Kate Morgenier presented for JP Morgan. Mr. Kauffman disclosed that his firm works with JP Morgan. Ms. Morgenier presented her partners Jennifer Ciullo and Alexia Gottschalch, which will also be presenting on behalf of JP Morgan. Mr. Kauffman asked to what they attribute the high level of redemption. Ms. Gottschalch answered that it is attributed to a significant equity market volatility that reflects in real estate redemption requests, and JP Morgan has a long window for redemption requests. Mr. Ross asked how do they get the liquidity. Ms. Gottschalch answered that they do not borrow money to pay out redemption requests ever, and there is a strong income return from this fund because all assets are well leased. Mr. Kauffman asked if they expect higher redemption requests in light of the rapid increase of the interest rate environment. Ms. Gottschalch answered no. Mr. Ross asked why shopping centers go in the world of Internet retail. Ms. Gottschalch answered that they track e-commerce and it becomes very crowded. She discussed that the fee is based on the size of the investor, and it is a singular simple fee with no acquisition fee. Mr. Johnson asked what is the income projected next year. Ms. Gottschalch answered income will be strong in the next year. Mr. Stanton asked about the wrong decisions that the organization has made through the year and what have they learned. Ms. Gottschalch answered not going into secondary markets and/or hotels.

iii. Consultant Discussion

Mr. West discussed the objectives of these interviews and their recommendations. He stated that their recommendation is increasing the target allocation exposure of Real Estate to 10%. He commented on how these managers can complement what currently exists at the Town of Palm Beach. Mr. West stated that their objective is to bring two excellent choices from which the Board will choose. Mr. Johnson discussed the difference between the firms. Mr. Amling asked Mr. Johnson if he agrees with both managers that real estate will outperform fixed income in a rising interest rate environment. Mr. Johnson answered that he agrees. Mr. Kauffman asked Mr. Johnson to explain what happened in 1993 and 1994 in the Real Estate market. Mr. Johnson answered that 1994 was the first year before 2013 when the Barclay Bond market was negative. Mr. West discussed the impact of rising interest rates and that Real Estate is a hard asset that benefits in an inflationary environment.

Mr. Madison made the motion to accept JP Morgan. Mr. Bradford seconded the motion. The trustees unanimously approved the motion.

D. Portfolio Adjustment Recommendations

Mr. Johnson asked the Board to make a motion to approve their recommendation on various items. He recommended reduction of the current emerging market equity exposure. He stated that the Town has two managers and they recommend removing the Acadian fund because of the higher fee and underperformance. He recommended decreasing the Vanguard total bond market index fund and increasing equity exposure commensurate with the allocation changes in the policy.

Mr. Stanton made the motion to adopt the recommendation made by Mr. Johnson. Mr. Bradford seconded the motion. The trustees unanimously approved the motion.

Mr. Johnson discussed the new contract with State Street and their renewal fee.

Mr. Ross made the motion to adopt 80 basis points for the current quarter and the performance base fee to go in effect January 1st. Mr. Stanton seconded the motion. The trustees unanimously approved the motion.

E. Investment of Town Contribution (Allocation Recommendation)

Mr. Johnson discussed the memo regarding the Town contribution of $8 million dollars and their recommendation. He stated that $5.5 million was moved into the investment portfolio and more money will be needed to come out of that portfolio. Mr. Linn discussed the agreement.

Mr. Johnson discussed that the auditor needs for State Street to provide information regarding the investment portfolio in order to comply with new GASB 72 reporting, and that State Street has offered to do the work and provide the report for a fee of $500.

Mr. Ross made the motion to approve the $500 fee for the GASB 72 Report. Mr. Amling seconded the motion. The trustees unanimously approved the motion.

F. Defined Contribution Report

Mr. Johnson recommended inviting ICMA to come to the next Retirement Board meeting.

VIII. Introduction of Actuary Pete Strong, Gabriel Roeder Smith & Company (GRS)

A. Valuation Procedure

Mr. Pete Strong introduced himself as the new actuary from Gabriel, Roeder, Smith to serve the Town of Palm Beach Board of Trustees. He discussed the valuation procedure and its components.

B. Payroll Increase Assumption

Mr. Strong discussed a matter of the assumption of payroll increase that is not acceptable by the state Division of Retirement. Mr. Strong stated that the Town of Palm Beach is using a 3.5% payroll growth rate assumption, and the state discussed with actuary Mr. Armstrong that the board should lower this assumption before it can be accepted. Mr. Ross inquired to what level it should be lowered. Mr. Strong answered 2.75%. Mr. Linn discussed that the state law says that you cannot exceed the past 10-year historical average. Mr. Strong stated that the last 10 years have been negative. Mr. Ross stated that payroll went down because of shrinkage in salary. Mr. Strong noted that the state looks at the economic situation of the Town. Mr. Ross asked how do you prove the future. Mr. Strong answered you cannot prove the future, but can only make assumptions of the future. Mr. Linn discussed that the state policy is to encourage more funding sooner into a retirement plan. Mr. Ross asked when did this come up. Mr. Strong answered that it was sometime within the past year. Mr. Hanes stated that typically there is a process going to the state for information. Mr. Ross commented that it would have been good to know and that the Board needs to know the problem. Mr. Strong stated that by him being close in proximity, he will be able to inform the Board of any problems going forward. Mr. Ross commented that the Board can be emailed with the information when needed.

Mr. Ross asked what is the difference between a 25 and 30-year amortization regarding the unfunded liability. Mr. Strong answered that reducing the amortization period to 25 years will cost an initial payment increase of about $200,000.

C. Services and fee agreement

Mr. Strong reviewed the Town retirement system's service and fee agreement with GRS.

Mr. Bradford made the motion to approve the agreement. Mr. Kauffman seconded the motion. The trustees unanimously approved the motion.

IX. Attorney Report, James Linn, Attorney

Mr. Linn had no comments.

X. Administrator's Report, William Hanes, Administrator.

Mr. Hanes discussed the report for payment of benefits.

Mr. Ross made the motion to approve the administrator's report. Mr. Bradford seconded the motion. The trustees unanimously approved the motion.

XI. Other business

none

XII. Adjournment

Mr. Ross made the motion to adjourn the meeting. Mr. Goldsmith seconded the motion. The trustees unanimously approved the motion.

Respectfully Submitted,

Brett Madison, Secretary
Town of Palm Beach Retirement Board