The Town of Palm Beach Retirement System
Board of Trustees
Minutes of May 15, 2015 Meeting

I. Call to order and Roll Call

Chair Pro-Tem Goldsmith called the meeting to order at 9:05 a.m. in the Town of Palm Beach Town Hall Chambers, 360 South County Road, Palm Beach, Florida 33480.

In Attendance:

TRUSTEES:
Gerald Goldsmith, Chair Pro-Tem
James McC. Wearn, Secretary
Wilbur L. Ross
Thomas G. Bradford, Town Manager
Robert Garvy
Brett Madison
Lieutenant Michael Marx
Detective Daniel Wilkinson

ALSO PRESENT:
William P. Hanes, Pension Administrator
Jane Struder, Finance Director
Danielle Olson, Human Resources Director
Rosemary Guillette, Segal Rogerscasey
James Linn, Attorney
Brad Armstrong, GRS

II. Administer the Oath of Office, Susan Owens, Town Clerk's Office

Mr. Goldsmith stated that the oath will be administered to Mr. Stanton at the next meeting because Mr. Stanton was previously scheduled to be out of the country and is unable to attend this board meeting.

Ms. Owens administered the oath of office to Mr. Brett Madison.

III. Election of Officers, Attorney Jim Linn

Mr. Goldsmith suggested the election of the officers be held at the next meeting when there will be two new members. Mr. Wearn agreed that a full board should be present. Mr. Bradford discussed his preference to wait until there is a full board present.

Mr. Wearn made the motion to wait until next meeting for the election of the officers. Mr. Bradford seconded the motion. The trustees unanimously approved the motion.

IV. Approval of Agenda

Mr. Ross made the motion to approve the agenda. Mr. Wearn seconded the motion. The trustees unanimously approved the agenda.

V. Public Comments

No public comments.

VI. Trustee Comments

Mr. Goldsmith commented that Mr. Garvy had notified the Administrator that he is resigning as trustee to this board, and he will be missed. He thanked Mr. Garvy for his service to the board. Mr. Garvy commented that he is disappointed that he must resign the board, and explained that he is a trustee of the University of Central Florida and Chairman of the Education Committee, and that state regulation prohibits him from serving on two boards at the same time. Mr. Garvy thanked the board for allowing him to serve.

VII. Approval of Minutes: February 20, 2015

Mr. Wearn made the motion to approve the minutes of February 20, 2015. Mr. Ross seconded the motion. The trustees unanimously approved the motion.

Mr. Hanes stated that he will be making minor corrections of the approved draft. He discussed that he will also include Mr. Linn as in attendance.

VIII. Financial Report and Disbursements, Jane Struder, Director of Finance

Ms. Struder presented the quarterly financial report through March 31, 2015.

Mr. Madison asked about the $6 million in DROP assets held at ICMA. Ms. Struder stated that this is the first year that the auditors required the section related to ICMA-RC holdings to be included in the report. She discussed that the assets held at ICMA-RC that were transferred over in January, 2015 are all in one pool. She noted that the remaining assets from people who have terminated DROP participation and have retired with accounts at ICMA will be liquidated out of those plans by July, 2015.

Mr. Wearn made the motion to approve the report and authorize the liquidation of $3.5 million dollars for quarterly benefit payments and expenses. Mr. Madison seconded the motion. The trustees unanimously approved the motion.

Mr. Ross made the motion to ratify the disbursement report. Mr. Wearn seconded the motion. The trustees unanimously approved the motion.

Mr. Goldsmith discussed issues from a recent Town Council meeting regarding the effect of retirement funding if the DROP is extended from 5 to 7 years. He commented that the correspondence that he received from Mr. Hanes that was a review by Mr. Armstrong stated that there is de minimus impact to the pension funds if the DROP period is extended. Mr. Hanes clarified that the Town Council has not passed anything yet and the proposal has been deferred until the next Town Council meeting. Mr. Hanes explained that no additional contributions are made into the retirement plan after commencement of DROP and after termination of DROP as there is no further liabilities assumed. Therefore there is no liability created from discontinuation of contributions. Mr. Ross commented that one reason the staff wants it is for the tax deferred extension benefit for the retiree. Mr. Hanes stated that the argument he heard at the Town Council meeting was that the Town would retain good experienced employees for a longer period with an extended DROP period. Mr. Goldsmith questioned if there is a financial effect on the pension fund. Mr. Hanes stated that he understood from the actuary that there will be no meaningful financial effect and if there is it will be minimal.

Mr. Linn made note that when someone terminates the DROP, they do not have to take a taxable distribution because they can defer it by rolling it into an IRA or another qualified account. He commented that the tax issue is not as significant as some of the other issues. Mr. Hanes added that it becomes taxable income when received by the member, and balances do not necessarily need to be rolled over to remain tax deferred as it can remain in the Town's tax deferred account.

Mr. Goldsmith discussed that the main concern of the Town Council is if there is any effect on the amount of money that would have to go from the town into the pension fund, and if there is any detriment by doing so. Mr. Armstrong discussed that there has been numerous changes to the interest credited to the Town's DROP. He commented that there is a trailing 5-years average method and the current actuarial assumption is 7.5%. Mr. Ross suggested the board recommend to the town council to credit the DROP what is actually earned.

Mr. Linn discussed that the reason for using a longer trailing average, rather than a quarterly basis average, was because of the guidance from the IRS on what will meet the required IRS tax threshold for a definitely determinable benefit. Mr. Ross suggested that since the IRS has to approve it anyway, why not propose the credit be provided on an actual basis instead of guessing. Mr. Hanes clarified that "definitely determinable benefit" is something required under IRS rules to be classified as a defined benefit plan. He commented that Ice Miller has suggested that we need to comply with the defined benefit plan standards because we are going from a Defined Contribution at ICMA-RC to a Defined Benefit plan when held by the Town. He stated that before December 31, 2014, we credited quarterly for Firefighters who held DROP or Share accounts with the Town plan, until it was recently changed because of the recent tax issues. He explained that the smoothing method makes it look more like a defined benefit plan. Mr. Wearn questioned if there is a difference when the calculations are done and when they get credited, and if it is affected by the 5 to 7 year change. Mr. Armstrong answered that it is not expected to, however, there could be periods when it impacts employer contributions upward and downward to a relative small extent, especially if the near financial collapse in 2009 were to repeat itself.

Mr. Wearn suggested that a memorandum should be written regarding this issue and presented to the Town Council. Mr. Goldsmith stated the retirement board should read the correspondence first and then decide what they should recommend to Town Council. Mr. Garvy stated that definitely there could be a short-term impact and it could be sizable. Mr. Linn stated that what he understands from Mr. Armstrong is that over the long-term there could be periods when there would be cost, but those will be offset with periods of increase, which would balance out over the long term. Mr. Ross stated that what Mr. Linn stated is true only if the same number of people contributes every single year. Mr. Armstrong agreed. Mr. Wearn commented that the board is not prepared to make a recommendation to the Town Council. Mr. Goldsmith stated that he wants the board to make an informed decision and present it to Town Council.

Ms. Struder asked Mr. Armstrong if there would be a cost if employees leave their assets in the plan until they turned age 60. Mr. Armstrong stated that is short term versus long term, and it absolutely will have an effect. Mr. Armstrong stated that the topic is wide-range and involves human resources. He

commented that it can impact the active healthcare costs because of an older employee population, and the mid-career employees may not see the same opportunities that may change their potential for promotion. He commented that these factors show that there are external effects that should be considered. Mr. Garvy stated that extending the DROP program presumably will retain stability in the senior employee base.

Mr. Linn suggested that in the absence of clear IRS guidance the best thing to do is to follow the tax lawyer's best advice to continue with crediting quarterly based on the trailing five-year average return. Mr. Goldsmith stated that there are two big questions that Town Council may wish to ask of the trustees. Is there any direct effect on the monies in our retirement fund? Is there any direct effect on the contributions that the council has to authorize for the retirement system? Mr. Garvy stated that the difference between a 5-year and a 7-year DROP program on the Town contributions seems relatively very small even in the event of a significant variation in the returns. Mr. Ross suggested presenting the council with a couple of models with options based on the different probabilities and unknowns.

Mr. Wearn made the motion to put the suggestion in memorandum form for response to the Town Council based on legal counsel and actuary advice. Mr. Goldsmith seconded the motion. The trustees unanimously approved the motion.

Mr. Bradford stated that the impact on the pension is only one of the variables relative to the overall issue of whether or not to increase the DROP period. He explained that some, but not all, of the additional issues being considered such as who this applies to, how long the town will do it, what is the internal and external impacts, are being considered.

IX. DROP procedures and online status, Jane Struder and William Hanes

Ms. Struder and Mr. Hanes presented the report, answered questions, and commented that the report will be provided to DROP participants.

Mr. Madison made the motion to approve the report. Mr. Wearn seconded the motion. The trustees unanimously approved the motion.

X. Actuarial Experience Report, Brad Armstrong, GRS

Mr. Armstrong presented the Actuarial Experience report. He stated that his hope is to take the complication from the bound report and instill it with his presentation. He explained that the purpose of an experience study is to measure the financial condition of the system, which is the same as is done with the annual actuarial valuation with existing assumptions. He commented that economic cycles are tough to figure out. He discussed as an example that if unemployment is running really high, then there is going to be lower rates of turnover because people tend to keep their jobs more so when there is higher unemployment.

Mr. Armstrong stated that the responsibilities of the Actuary are to look at the different groups independently. He discussed that economic assumptions are matters that happen to money, and decided by the trustees. He then discussed that the term demographic represents decisions that are made by

people, like a disability. He commented that disability experience is hard to measure in a large group plan. He discussed that economic assumptions include Price Inflation, Investment Return, and a comparison between assumed experiences with actual experiences. Mr. Armstrong discussed that the 2014 Social Security report assumes an intermediate assumption for price inflation to be 2.5%. Mr. Ross asked how a police officer improves his productivity. Mr. Armstrong stated that advances in technology help measure the productivity, and there is a small amount of room for increase in productivity in the police department. He commented that firefighters are harder to measure because a lot of what they do is more related to providing care and saving lives.

Mr. Ross discussed that the chart on page 10 shows the price inflation assumption of 2.77% for the last 30 years, and yet the whole world is struggling for 2% right now. Mr. Armstrong explained that the investment consulting firms identified in the report are making capital assumptions reflective of more forward looking forecasts, and more so than past averages. He discussed that the recommendations are in the range of 2.26% to 3.25%. Mr. Garvy questioned why wage inflation was increased if there's no expectation of an increase number of employees. Mr. Armstrong agreed but stated that there is still going to be wage increases. Mr. Armstrong explained that in 2014 there was wage increase for the year, even though for the whole past 5-year period there were no increases in payroll. Mr. Garvy stated that the expectation is not that the increase is 0, but questioned why there is a 3.5% assumption on wage inflation. Mr. Armstrong explained that plan A benefits are frozen and has no effect, and Plan B only affects the active employees. He discussed that the assumption is related to projection of salaries and lower liabilities for future retirees. He added that the unfunded liability is paid based on dollar amounts, and the town contribution dollars are expected to go up 3.5% per year.

Ms. Struder stated that wage growth has been stagnant because of turnover. She presented that information regarding growth in salary for the next 5 years is expected to be below 2%; but that it then is expected to increase to 3% once employees leave the DROP. She stated this does not account for promotions, whereas Mr. Armstrong's recommended wage assumption does include potential for promotions and wage increases. Mr. Garvy asked for clarification on how wage inflation impacts on payroll amortization. Mr. Armstrong stated that the expectation is that if $1 is invested it will grow at 7.5%. He discussed that even if there is inflation in the future the town will be able to pay. Mr. Ross asked from the report what it is that drives up the town contribution rate while decreasing the funded ratio. Mr. Armstrong stated that it is the adoption of the new mortality table. He explained that it is primarily the legacy aspect of plan A, which represents the frozen benefits. He stated that regardless how long the employee has been in the DROP, the longer people live, the retirement liability grows, and the large ticket items are affected. Mr. Ross asked how much has the mortality assumption changed. Mr. Armstrong stated that life expectancy has increased by 3 to 4 years and that the recommendation is based on adoption of the mortality table used by the Florida Retirement System.

Mr. Ross made the motion to approve the GRS recommendation of new assumptions. Mr. Wearn seconded the motion. The trustees unanimously approved the motion.

XI. Investment Report, Rosemary Guillette, Segal Rogerscasey

A. Asset Allocation and impact of experience study

Ms. Guillette stated that matters of the experience study and the new mortality table is being coordinated between the actuary and Segal Rogerscasey, and the impact on asset allocation will be presented at the next meeting.

B. Quarterly Performance Report

Ms. Guillette reviewed the performance report for the first quarter of 2015. She reviewed index performance for each asset class and the returns. She commented there was a large difference in performance between growth stock and value stock for the quarter. She discussed that there was positive bond returns.

Ms. Guillette reviewed the current target allocation versus actual allocations from the asset allocation model for each asset class represented. She mentioned that the plan is about 9% over in equities, and private equity will need to draw down the money that will happen over time. She commented that between last quarter and this quarter, money was allocated for Vanguard REIT index to complete some real estate exposure at 4%. She discussed that the board had decided at the last quarterly meeting to increase allocation to commodities, and that it has been done. She mentioned that the board had decided to hire JP Morgan for venture capital, which has not been done to date and the contract is still pending. She noted that Oaktree had previously been selected as a real estate manager, but the board had voted not to approve Oaktree for reasons of contract issues.

Ms. Guillette reviewed the performance of each manager. She stated that the total portfolio value as of December 31, 2014 was $202,986,640, and as of March 31, 2015 it was up to $211,443,638. She commented that the composite performance of the funds for the quarter ending on March 31, 2015 were up 2.01%. She commented that the retirement fund did underperform slightly over the quarter and over the one and two-year period, but have outperformed since inception. She commented the domestic and international equities did very well for the quarter, and that emerging markets, fixed income, commodities, and real estate underperformed for the quarter. She discussed performance for each fund manager.

Mr. Goldsmith asked if the fund Oaktree, who did not accept our contract terms, was eliminated. Mr. Linn clarified that it was eliminated because Oaktree did not want to accept fiduciary responsibility status. He stated that JP Morgan took the position that for a fund of our size they will not accept fiduciary status. Ms. Guillette stated they are experiencing contracts failing all over the place because fund managers are not agreeing to fiduciary responsibility status. Mr. Wearn stated that this must be a supply and demand situation. He commented that the demand for their products must be so high that they can dictate their terms. Ms. Guillette agreed. Mr. Wearn stated that he believes that the board should require that managers agree to fiduciary responsibility, and when a replacement is considered we should not interview with anyone that is not willing at the outset to accept our two primary requirements of fiduciary responsibility status and that lawsuits be filed in Florida. Mr. Ross asked about JP Morgan not accepting fiduciary responsibilities. Mr. Linn stated that the bottom line is that JP Morgan will not accept fiduciary responsibility due to the size of our fund. Mr. Garvy asked about the company that came in second at the last meeting. Mr. Hanes named the three firms that are believed to be the strongest, Horsly Bridge, Performance Venture Capital and JP Morgan. Mr. Garvy and Mr. Ross acknowledged they were impressed with the performance of Performance Venture Capital.

Mr. Goldsmith made the motion to approve Performance Venture Capital instead of JP Morgan. Mr. Wearn seconded the motion. The trustees unanimously approved the motion.

Mr. Linn requested that the board allow him to talk to JP Morgan one last chance to see if they will accept fiduciary responsibility. Mr. Goldsmith and Mr. Wearn agreed to amendment of the motion to do so. Mr. Wearn made the motion to approve the amendment to have a predicate inquiry to see if JP Morgan accepts fiduciary responsibility, and if not to move to a contract with Performance Venture Capital. Mr. Ross seconded the motion. The trustees unanimously approved the motion.

C. Oaktree

Ms. Guillette confirmed that the loss of Oaktree will require another search for another manager. She discussed that she will bring three companies to interview at the next meeting if the board agrees. Ms. Guillette indicated she will send information to the trustees over the next week or so regarding the managers that could be invited to the meeting for interview at the August 21 meeting. Mr. Goldsmith stated that the board will let Mr. Hanes know which three companies they would like to interview after they have received the information, and will arrange their presentations at the next meeting. Mr. Hanes suggested that Segal Rogerscasey inquire with the managers about accepting fiduciary responsibilities and that any lawsuits be held in Florida before selected for presentation and prior to the board interviews.

Ms. Guillette discussed the issue of fees paid to private equity managers. She stated that she believes the fees paid by this plan are reasonable, and that the plan has strong private equity managers. Mr. Ross asked if the private equity funds are fully offsetting the manager fees collected. Ms. Guillette stated that she does not know about this board's private equity funds specifically, but that she will find out and give the trustees an answer.

Mr. Garvy talked about Goldman Sachs low performance and that it is time the board consider to take action.

Mr. Ross made the motion to cut the allocation with Goldman Sachs in half. Mr. Garvy seconded the motion. The trustees unanimously approved the motion.

Mr. Ross moved to amend the motion to have the funds move one-half of the current allocation at Goldman Sachs to the same asset class at Vanguard. Mr. Garvy seconded the motion. The trustees unanimously approved the motion.

Ms. Guillette discussed matters of overlays. She stated that if the board is really interested, then the board should bring in someone who is well qualified. She stated that it is very expensive, and not worth the cost paid. Mr. Ross asked if Ms. Guillette could send the trustees written material so that the trustees can educate themselves about overlays. Mr. Guillette agreed.

XII. Attorney Report, Jim Linn, Attorney

A. Physician's Report of Reexamination

B. Retiree's Report of Continuing Disability

Mr. Linn prepared a form for a physician to re-exam a disabled member and a second form for the retiree to report for continuing disability. He commented that the retiree will be required to complete the form and the board will decide if the person needs to be re-examined. Mr. Wearn commented that he had reviewed the forms with legal counsel and that the forms accomplishes a good purpose for the board and will keep the board from placing too much of a burden on the retiree on an annual basis. Mr. Hanes discussed that the vast majority of current disability recipients are beyond the age of normal retirement. He suggested that the board implement the new forms and procedure going forward with the disability applicants after the implementation of the new procedure, and not to re-examine those currently on a disability retirement. Mr. Madison asked if the re-examination would stop at retirement age. Mr. Hanes clarified that he did not believe the review should continue after the person is normal retirement age.

The trustees discussed and agreed without motion that once the disability recipient reaches normal retirement age that further review will no longer be applicable.

Mr. Wilkinson asked if the medical information requested on the form is limited to conditions related to the member's disability. Mr. Linn explained that the form is not limited. The form is to the treating physical, but no limitations on the medical information requested. Mr. Hanes explained that it is not limited because they may have a disability retirement because of primarily one condition, but additional limitations may be a contributing cause of the particular claim for disability. Ms. Olson, Human Resource Director, discussed the procedures, and agreed that the form should remain broad in order for the physician to have all the medical evidence, and to enable the board to perform their fiduciary duties.

Mr. Wearn made the motion to approve the forms and procedure, but only to apply to future disability retirements. Mr. Madison seconded the motion. The Trustees unanimously approved the motion.

C. IRS Determination Letter Request Status

Mr. Linn discussed matters of the board's request for a determination letter and voluntary correction program from the IRS. He stated that the paper work had been prepared by Tax Counsel Ice Miller to submit, but is waiting for Mr. Hanes to sign off on the various forms. He commented that the board needs to provide additional authorization for Ice Miller's legal fees and for the IRS filing fees. He discussed that the IRS filing fees are going to be a total of $2,875.

Mr. Ross made the motion to approve paying of the IRS filing fee. Mr. Wearn seconded the motion. The Trustees unanimously passed the motion.

Mr. Linn discussed that the board had previously authorized paying the legal fees not to exceed $57,000 at the November meeting. He stated that we have received and paid invoices from Ice Miller to date at approximately $67,000. He discussed that there will be additional fees, but that he does not believe it will be significant. Mr. Linn recommended that the board authorize an additional $30,000 above what has been paid. Several trustees expressed concerns over the significant costs that have been incurred. The board inquired about the involvement and hours required to perform the work. Mr. Linn discussed that the increased hours is because the IRS has not been clear so Ice Miller is spending more time on the project than was originally expected. Mr. Wearn asked Mr. Linn if there is an estimated amount of time needed. Mr. Linn stated that Ice Miller has not provided that information. Mr. Hanes stated that there are many people at many levels working on the project, and that there are several employees of the Ice Miller firm doing different work on the project. Mr. Garvy and Mr. Ross expressed that it is very expensive. Mr. Bradford requested when the filing will be complete and the board can expect to get a final determination letter. Mr. Linn discussed that there has been quite a bit of back and forth with the IRS, but he believes that it will be several months before receiving a final determination letter. Mr. Linn stated he will seek an estimate of hours from Ice Miller.

Mr. Ross made a motion to pay the original cap. Mr. Hanes explained that the expenses already incurred are already over the cap. The motion was not seconded. Mr. Linn explained that other retirement plans are having the same or similar issues with the IRS on the matter of the Defined Contribution DROP. Mr. Wilkinson asked if a lump sum payment by contract would be appropriate for this type of service. Mr. Linn answered in the negative. Mr. Wearn made inquiry with Mr. Linn regarding if we are ready to file, and commented if so the board would seem to be at a level of compliance until the IRS responds with a problem. He suggested that we file with the IRS and wait for their response, and without authorizing additional expenditures. He suggested that any response be returned to the board.

Mr. Ross made a motion to approve the balance owed to Ice Miller above what has already been paid. Mr. Wearn seconded the motion. The Trustees unanimously passed the motion.

D. Final State Legislation

Mr. Linn discussed the matter of the state legislature's mandate to use a latest generational mortality table. Mr. Bradford discussed that the Florida Retirement System (FRS) has already adopted the newly mandated mortality tables. Mr. Linn discussed that FRS experienced an 18% return performance in the prior year, and was funded at an 86% rate. He discussed that the relative contribution rates for that plan is less than other municipal plans because of the lower unfunded liability.

C. (Continued)

Mr. Bradford requested a clarification on what Ice Miller is being told to do before the next meeting. Mr. Linn stated that he will tell Ice Miller that the board is unwilling to authorize more fees, and ask them what they believe is going to be the total in order to get through the determination letter process. Mr. Wearn discussed that the retirement administrator should serve as an alternate contact, and any remaining inquiry from the IRS can be taken to the board by the retirement administrator. Mr. Wearn stated the retirement administrator will not need to act as a lawyer, but be a referring person who will ask the IRS to put questions in writing and later present it to Mr. Linn or the board. Mr. Linn stated that the board hired Ice Miller to work with the IRS on these tax issues regarding this governmental plan, and expressed that he believes the board will want Ice Miller to work with the IRS because that is what they do. Mr. Ross expressed that he has no problem with Ice Miller doing the work, but that he sees no reason it takes hundreds of hours on this application. Mr. Wearn stated he does not see a problem with the alternate approach for the Town's retirement administrator being the main contact, and it will not impede on their (Ice Miller) reputation.

The board directed without motion that Mr. Hanes and Mr. Linn will act as the alternate administrators as directed by the board.

XIII. Retirement/Benefits, William Hanes, Administrator

Mr. Hanes briefly presented the retirement benefits report.

Mr. Wearn made the motion to approve the report. Mr. Madison seconded the motion. The trustees unanimously approved the motion.

XIV. Administrator Report

Mr. Hanes reported that Mr. Garvey is vacating his board position so an appointment needs to be held to fill his position. Mr. Bradford concurred that the appointment will be made at the July Town Council meeting. Mr. Hanes commented that there should be a full complement of trustees at the August 21, 2015 meeting.

Mr. Hanes discussed that Mr. Goldsmith will be making the retirement board presentation at the June 9, 2015 meeting of Town Council. The trustees concurred without motion.

XV. Other Business

None

XVI. Adjournment

Mr. Ross made the motion to adjourn the meeting. Mr. Bradford seconded the motion. The Trustees unanimously approved the motion.

Respectfully Submitted,