Town of Palm Beach Retirement System
Board of Trustees
Minutes of November 17, 2017

I. Call to Order and Roll Call

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

In Attendance:

TRUSTEES:
Daniel Stanton, Chairman
Tom Bradford, Town Manager
Brett Madison, Secretary
Jeffrey Amling, Trustee
Brad Kaufman, Trustee
Ed Carter, Trustee
Gerald Goldsmith, Trustee
Michael Marx, Trustee
Dan Wilkinson, Trustee

ALSO PRESENT:
William P. Hanes, Retirement Administrator
Jane Struder, Finance Director
David West, AndCo Consulting
Danielle Olson, Human Resources Director
James Linn, Attorney

II. Approval of Agenda

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

III. Comments by Trustees

None

IV. Public Comments

None

V. Approval of Minutes, August 18, 2017

Chairman Stanton commented there was one word incorrect that needs correction from the minutes. He identified on page 4 that the word underwhelming should be entered as underweighted.

Mr. Bradford made the motion to approve the minutes with the amendment offered by Chairman Stanton. Mr. Wilkinson 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 through September 30, 2017. She stated that the report has unaudited numbers and the audited numbers will be provided at the next meeting on March 2. She provided the financial details from the written report and indicated there was no need to transfer additional money from managers for payment of next quarter's benefit and expense payments.

Mr. Kaufman made the motion to accept the disbursements from the report for the quarter. Mr. Bradford seconded the motion. The trustees unanimously approved the motion.

VII. Presentation on Trustee Legal Powers and Duties as a Fiduciary, James Linn, Attorney

Mr. Linn discussed an overview of the Retirement Board powers and duties. He stated that the board was established by the Town Council as a legal entity with the authority to administer the retirement system for the benefit of the members, retirants, and beneficiaries. He commented that the board has the authority to bring and defend lawsuits, and the primary function of the board is directing the investment of assets of the retirement system as provided within the investment policy statement. He stated that board members are fiduciaries of the funds, which means trustees are charged with administering the fund and directing the investments in the best interest of the members of the retirement system pursuant to the prudent person rule. He stated that the retirement plan is qualified under the Internal Revenue Code, meaning the plan growth is not taxed until paid out to members of the plan. He stated there is a range of rules and regulations that govern qualified plans. He reminded the board that tax council previously recommended changes that have been enacted by the Town to ensure qualified status, and with one more change remaining, and to be adopted.

Mr. Linn stated that the issue he reported on at the prior meeting regarding the members exceeding the Sec. 415 excess benefit has been resolved. Mr. Goldsmith commented that the board cannot legislate.

Mr. Carter asked if decisions made regarding the assumptions are the purview of the Retirement Board. Mr. Linn answered that the Retirement Board that determines the assumption, but noted an exception under the code that the rate of return assumption requires approval by Town Council. Chairman Stanton asked if there is anything that has happened in the past with the Retirement Board that was close to a breach of fiduciary duties. Mr. Linn answered no.

VIII. Town Council September 19, 2017 Annual Retirement Report, Chairman Dan Stanton

Chairman Stanton commented on the annual retirement report he presented to Town Council on September 19, 2017, and that two alternatives for additional funding were provided to Town Council to address the unfunded liability. He stated that the Town Council approved the option of an annual fixed $5.42 million to be allocated by the Town each year in addition to the legally required amount. He stated there were many questions asked by Town Council, and noted one item decided is that a special Town Council meeting will be held annually to discuss retirement issues. Mr. Hanes commented that as a part of the upcoming annual Town Council meeting with the board, the actuary has been asked to provide a new 10-year funding forecast based on the most recent 2017 fiscal year investment performance.

IX. Investment Report, Dave West, AndCo Consulting, LLC

Mr. West stated that he had good news regarding the asset allocation, and the pension assets were placed in the right places over the year to capture very good returns. He discussed 3 agenda items (1) AndCo firm update, (2) the review of the Investment Report, and (3) the recent recommendation for the Town to make additional contributions. He introduced his colleague, Misha Bell, who is in charge to reporting. He discussed the rebranding and equity ownership with the AndCo group.

Mr. West reviewed the Quarterly Investment Report. He gave an overview of the most significant items that impacted returns over the 2017 year, including the investment progress and what needs to be done going forward. He noted a huge improvement in active management performance, and commented that long term interest rates have come down while bond prices have gone up. He noted that we have moved into the next phase of the recovery, and there is a global recovery resulting in international equities being the best performers over the last two quarters. He stated that the managers that have reported to date represents 85% of the portfolio, but the report does not include current private equity and private equity real estate investments because of delays in valuation from those asset classes. He noted that the fund performed at 10.92%, and would probably perform at 12.72% if all reporting was current as of today.

Chairman Stanton questioned the inconsistency between the total fund performance versus the total fund policy performance over the last two to three years where policy has outperformed the total fund. He asked

Mr. West his thoughts on that issue. Mr. West stated that it was largely due to management performance deficiency due to original asset allocation and policy construction. Mr. Goldsmith noted that we had a serious lag in liquidation of funds during the year. Mr. West agreed that liquidation with the many illiquid asset holdings was a challenge. Chairman Stanton questioned the alternative policy total of 22%. Mr. West answered that it was derived from the investment policy statement that produces an assigned custom benchmark with an inflation plus adjustment. He noted it is a constant earnings rate that is high. He commented he is using the peer group as a secondary policy measure along with the primary fixed policy. Chairman Stanton suggested relooking at how the number is derived if this portfolio keeps underperforming relative to policy. Mr. West agreed that the number is high and they will go back and confirm the numbers.

Chairman Stanton commented on the manager Thompson, Siegel & Walmsley (TSW) SMID fund, which changed their name to hide their bad management performance. He asked if AndCo is monitoring the changes in managers. Mr. West answered by comparing the managers and giving an overview of their management of performance. He commented that AndCo's efforts to date have been to set up the asset allocation of the portfolio, which is by far most impactful to performance, and going forward he believes AndCo can get to business as usual and will be able to zero in on monitoring the manager performance. Chairman Stanton commented in the market that we are in that value stocks are underperforming growth, and the fact that they are lagging is not a surprise. He stated his real issue is if they are lagging more than what they should because of poor performance. Mr. West stated that the index applied here, which is the Russell 2500 value index, are an apple to apple comparison. He added that according to this benchmark, the manager is lacking. He commented that they are tracking the full manager history that gives a long-term look, and that they are now at the point where they can be more focused on managers. Chairman Stanton requested a more in-depth analysis of their performance and to discuss the construction of the alternative benchmark for the next meeting. Mr. West made additional comment that Artisan performance is under the radar screen and he will bring to the next meeting for discussion for possible replacement.

Mr. Goldsmith asked who sets the benchmarks. Mr. West answered that is not arbitrary and AndCo sets the benchmark and work with managers to meet the expectations. Mr. Linn asked if the benchmarks are reflected in the policy statement. Mr. West confirmed.

Mr. Goldsmith inquired of Mr. West how well we performed overall. Mr. West stated that the benchmark is 7.3%, and we performed admirably well, especially considering the difficulty of making changes because of caps imposed by the legacy investment policy statement, and that it took Town Council time to adopt the change made to the new investment policy statement.

Mr. Kaufman discussed with Mr. West the issue of performance differences between active and passive, and commented that performance depends on consideration of the starting point. He stated that if you look at the S&P performance over time, it will outperform almost every active manager. Mr. West stated that he takes Mr. Kaufman's point to be that it is about the point to point measurement, so if they came in at a good starting point, it could bias the point to point data. He commented that what they are trying to do on the way is to be cognizant of the rolling returns and style specific in comparisons to be fair, and that it is imperative to be cycle aware. He commented that we have come through an exceptional long period of time where indexing has prevailed as a style of investing in domestic equity. He stated it is his hope that we are at the point of inflection when the return to fundamental investing will provide a more fertile ground for active managers to bring value to the table, and historically investors will be better protection in down markets.

Mr. Bradford made inquiry regarding the board's role with placing managers on a watch list. Mr. West commented that AndCo reviews on a quarterly basis a very long list of managers they work with, and that it is not usually an action matter for the board to approve. Chairman Stanton requested that Mr. West provide the board a list of managers of this fund that AndCo is actively watching. Mr. West indicated the watch list of managers is typically related to compliance, and he will bring to the board to discuss with any recommendation from which the board will decide whether to ride it out or take some action. Mr. West commented that board action does not come until after AndCo has taken managers on a watch list to the board with a recommendation for action. Chairman Stanton asked if Mr. West will provide the board a list of managers being watched, and to distinguish those that are legacy managers inherited when AndCo was hired from those managers that were recommendations from AndCo and have been added to the portfolio by action of the board.

Mr. West updated the board on cash flow of the plan. He indicated that the Mesirow sale balance of $8 million from the June 30, 2017 quarterly report failed to show, and has been added to the current September 30, 2017 report.

Mr. Kaufman asked why there is still $401,000 in Mesirow. Mr. West answered that it represents a 10% hold back at liquidation, which is an industry standard. He commented these funds will be released after Mesirow clears their books, and their statements are audited.

Chairman Stanton asked about the 60% in management fee that appears to be paid to one manager, Oakmark. Mr. West answered that it appears to be some catch up in that number. Chairman Stanton asked Mr. West to review the item and report back to the board. Mr. Carter commented it looks expensive. Mr. West agreed that he will review and report back to the board.

Mr. West reviewed the Asset Allocation chart as of September 30, 2017. He stated that we are basically very close to where we need to be in complying with the target allocation, noting some strategic overweighting and underweighting in certain asset classes, and stated there are no recommendations for changes at this time. He commented that the plan is well positioned going forward. Chairman Stanton stated that Town Council will want to know where Mr. West plans that that the new Town allocation of $5.42 million will be applied. Mr. West answered that there is only one investment left to be funded. He recommends moving those funds to the Vanguard Domestic Bond Index Fund. Mr. Bradford asked why international is out. Mr. West answered that there is currently a good overweight with International right now, and AndCo recommends continuing at the current level of overweight with non-Domestic.

Mr. Kaufman made the motion for the incremental $6 million dollars of investable income be invested in the Vanguard bond index fund. Mr. Goldsmith seconded the motion. The trustees unanimously approved the motion.

Chairman Stanton commented that he hopes that AndCo does not give up on Hedge Funds and that at some point there will be a period of outperformance, and that it is worthy to keep on the radar. Chairman Stanton requested that if and when AndCo sees opportunities in that space with a changing environment, it would be something the board would like to hear. He commented that intuitively it doesn't seem possible that going forward there would not be outperformers in the space. Mr. West agreed, and stated it would be on the radar screen which would be a normal function anyway. Mr. West commented that the first function might be to find the best performing Hedge Fund, and the second function would be to look for Hedge Funds with good returns and lower volatility. He stated that the return expectation for that group would be a mix of equities and bonds. He stated this to be the function of current funds in this space. He reminded the board that Hedge Funds have outperformed fixed income, and has served as a source of capital while creating diversification. Mr. Carter suggested that it is important that AndCo clean up the policy with regard to the alternative space as previously discussed. Mr. West stated that he will place this as an action item for the next meeting.

Chairman Stanton stated he has written down four matters for Mr. West to address at the next meeting as follows: (1) More definition on policy for alternatives; (2) more information on TSW; (3) Oakmark management fee from cash flow chart, (4) Managers of the Town of Palm Beach recommended since AndCo, and the legacy managers AndCo would not be recommending if they were not already active with the plan.

X. Attorney Report, James Linn

Mr. Linn reviewed an issue previously discussed with the board related to a former actuary for the plan that had not discovered the excess benefit received by a retiree of the Town per the Internal Revenue Code, and neither did the actuary note one member who will exceed the limit in the future. He commented Actuary Strong discovered the two individuals with regard to exceeding the benefit limit, and the Town has negotiated a settlement with GRS whereby GRS will pay $68,000 that will cover the back payments that is required to be paid back into the pension trust from the current retiree benefit payments. This is in addition to other legal and Town fees. In addition, the Town has adopted an emergency ordinance that establishes a "preservation of benefits" plan that the Federal Internal Revenue Code allows for governments to enact in order to accommodate for an excess payment of benefit so that when an employee has not been advised of the excess benefit limitation that the retiree will be made whole. The contribution made by the Town toward the retirement plan is reduced based on reduction in liability, but then the Town must pay into a separate account for paying the liability associated with the excess benefit. He concluded that GRS stepped up and did the right thing with no additional cost to the Town or retirement plan, and the two employees will be made whole for receiving the excess benefit amounts.

Mr. Carter inquired about the current 415 limit. Mr. Linn stated that the current limit is $215,000 at age 62, however, the limit is reduced for people retiring prior to age 62.

XI. Administrator's Report, William Hanes

Mr. Hanes presented his report that included one retirement.

Mr. Madison made the motion to ratify the retirement based on the report. Mr. Bradford seconded the motion. The trustees unanimously adopted the motion.

XII. Other Business

None.

XIII. Adjournment

Mr. Goldsmith made the motion to adjourn. Mr. Bradford seconded the motion. The trustees unanimously adopted the motion.

Respectfully Submitted,

Town of Palm Beach Retirement System
Board of Trustees
Brett E. Madison, Secretary