Town of Palm Beach Firefighters' Retirement System

MINUTES OF MEETING HELD
February 23, 2006

I. CALL TO ORDER

Chairman Richard Krock called a meeting of the Firefighters' Retirement System to order on behalf of the Board of Trustees at 9:04 AM on February 23, 2006, in the Town Council Chambers. Those persons present included:

TRUSTEES	OTHERS
Richard Krock, Town Appointed Trustee	Bonni Jensen, Attorney
Peter Geisler, Town Appointed Trustee	Scott Baur, Administrator
Mike Hayes, Elected Trustee	Ramelle M. Hieronymus, Prime Buchholz
John Cuomo, Elected Trustee	Sean Higman, Prime Buchholz
Robert Jaffe, Board Elected Trustee	

II. APPROVAL OF AGENDA

The Trustees accepted the Agenda without modification.

III. APPROVAL OF MINUTES: MEETING OF NOVEMBER 10, 2005

Mr. Hayes made a motion to accept the minutes for the meeting of November 10th, 2005. Mr. Geisler seconded the motion, approved by the Trustees 4-0.

IV. INVESTMENT MANAGER PRESENTATIONS: REAL ASSET MANAGERS

A. GUGGENHEIM - KAREN CALBY

Ms. Calby stated that Guggenheim Real Estate PLUS is "an open-end, actively managed strategy which provides a diversified real estate portfolio. The product has quarterly liquidity. The real estate is diversified across the United Stated. The product is benchmarked representative of the broad institutional real estate market. Target returns, before fees and expenses, of 200-400 basis points over benchmark (70% NCREIF/30% NAREIT). The portfolio is actively managed with focus on "search for value" to respond to changing investment conditions in the real estate market. Much of the compensation of both Guggenheim Real Estate and their investment partners is incentive-based (calculated by fund performance relative to benchmark).

The portfolio is actively managed to seek value by considering property type and geographic weights, public/private arbitrage, portfolio evaluation, entrepreneurial execution, value-added, and liquidity/leverage for structures.

Risk control focuses on diversification by public or private market, property type, and geography with sector weightings no more than 150% of benchmark. Leverage is monitored and total leverage cannot exceed 52.5% and the portfolio does not invest in blind pools, raw land, private development companies, or international transactions.

Currently the portfolio is allocated about 30% in public holdings and 70% in private holdings. Ms. Calby reviewed both public and private holdings noting that the list of properties comprised only about 35% of the total portfolio.

Finally, Ms. Calby reviewed the management team for Guggenheim.

Peter Geiseler asked about the industry standard for leverage. Karen indicated that the direct ownership typically has 60 – 85% leverage, while developers can go even higher. She noted increased leverage adds to volatility as property values fluctuate.

Guggenheim has a 6-quarter lockup on the initial investment. The portfolio was founded in 2001 and net returns since inception are 15.64% compared to the benchmark of 15.04%.

The standard base management fee for institutional investors is a base of 60 basis points and a 20 basis point incentive fee over benchmark, and execution fees. Mr. Geisler asked who values the properties. Guggenheim does full appraisals over 1 – 3 years with quarterly updates to establish trading values.

John Cuomo asked about timing for investment in real estate since valuations seems high. Ms. Calby indicated that the residential priced higher than commercial with some areas of the country more overpriced than others. She recommended wide geographic diversification. Guggenheim will acknowledge a fiduciary in their contract with the Pension Fund.

B. <u>WELLINGTON ASSET MANAGEMENT – GARY ELIAS & JESSICA OLESON</u>

Wellington has about $500 billion in assets as a privately held company. It was commented that the SEC began a review of trading practices by Willington in 2005, which is incomplete but has no adverse findings. About $90 billion of assets are managed on behalf of public funds. Wellington creates a portfolio of diversified inflation hedges composed of many different types (real estate and natural resources) of real assets. Jessica talked about energy investments and demand created by China as example. The manager has a goal to return the CPI to + 5%, with a portfolio that includes inflation protected fixed income securities, commodities, and other assets. Overall long-term equities provide the strongest terms. Commodities can outperform at times though in the long-term the commodities will not have as high consistent returns. Jessica reviewed the team that manages the portfolio.

The portfolio has a one-year track record with returns of 26.5%, compared to 20.2% for the composite benchmark and 8.5% for the CPI + 5. Wellington believes the current trend will continue for rising inflation therefore commodities should continue to outperform.

The product has about $3.8 billion and it will close the fund at $5 billion.

Mr. Krock asked about the difference of the existing product and longer-term (3 year) track record. The other product has less in commodities, more in fixed income, and equities with investments that include small-cap stocks. Mr. Krock also asked about trading activity around asset allocation weightings to target weightings that vary 1 – 3%v per month.

The fee is 90 basis points with a minimum investment of $5 million. If the Retirement System invests less than $5 million, Wellington will charge a fee based on management of $5 million. Portfolio components have underlying benchmarks and the portfolio itself does not have a benchmark other than the CPI +5.

Wellington would accept fiduciary responsibility.

V. INVESTMENT MANAGER PRESENTATIONS: REAL ASSET MANAGERS

A. ARCHSTONE - JOE PIGNATELLI, PRESIDENT & CO-PORTFOLIO MANAGER

Archstone Partners, L.P. began investing on January 1, 1991 with their sole business being a fund of hedge funds. Total assets under management is $2.5 billion in four strategies.

Archstone believes in diversification, by modern portfolio theory, compensation tied to investment performance, and consistent performance. The investment objective is to protect capital during declining markets while participating during market advances; to build capital be earning premium of 600 basis points over the risk-free rate (Treasury bills) over the course of a market cycle; to achieve returns with low volatility; and to minimize the possibility of capital loss.

Management includes directional long/short strategies (60%) and non-directional market strategies (40%). Archstone manages as a fund of funds. The portfolio is transparent to show holdings in other hedge funds. Archstone has a strong due diligence process that focuses on the people doing the investing, the process and the performance. Archstone does not invest in any black boxes and the manager also checks on the assets claimed by the other managers included in the portfolio. Mr. Pignatelli characterized this fund as a hybrid comparable to Pine Grove or Meridian.

Mr. Jaffe disclosed he has family involved in Archstone.

B. AETOS - DAVID TONKOVICH & MICHAEL KLINE

Mr. Kline is a portfolio manager that focuses on risk management. Aetos is owned exclusively by investment professionals, and the firm works only for institutional investors. Total assets under management is $8 billion with $3 billion in hedge fund of funds. The firm also manages private equity and real estate. Mr. Tonkovich reviewed the experience of the management team. All the portfolio managers had part fiduciary responsibilities. 40 % of their clients are corporate and public pension plans with the other 60% being endowments and foundations.

Michael Kline stated that the portfolio is concentrated by manager. Strategies in the portfolio include market neutral strategies (15%), arbitrage (45%), long/short strategies (35%), and a distressed fund (5%).

For the past 12 months the fund returned about 5.8% in a lower volatile market environment. Aetos is transparent and divulges managers where portfolio is currently invested.

Michael Kline explained the investment philosophy. Aetos will customize strategies to individual clients. Manager selection begins with fundamental macro-economic research. Manager evaluation, portfolio construction, and re-evaluation. Risk management focuses on manager risk, operational risk, strategy risk, and quantitative risk. The portfolio considers liquidity driven strategies a s opposed to skill driven strategies. The liquidity driven strategies really give some insurance to the portfolio. Aetos looks for manager with an understandable process before going through an exhaustive evaluation of managers. Aetos monitors every manager in the portfolio monthly.

Aetos has a $1 million minimum investment requirement with a one year lock-up period and quarterly liquidity thereafter. Aetos will also accept fiduciary liability on behalf of the Retirement System.

Robert Jaffe also has family associated with Aetos.

VI. NORTHERN TRUST: INVESMENT MANAGEMENT OPTIONS – KRISTINA VAN LIEW, CIMA & PERRY E. BROWN

Northern Trust is the 8th largest institutional money manager, 3rd largest manager of managers and custodial services. Northern has $2.8 Trillion in assets in custody. Northern has about 30% share in key markets, $30 billion in fund of funds approach.

Northern does not use its own managers in the manager of managers approach. Northern develops close relationships will all of their clients. They have a local public clients as well. Ms. Van Liew reviewed issues facing plans today including the need to generate returns.

Northern provides accountability and will acknowledge fiduciary responsibility. Cost and fees are also important, particularly in a low return environment. This plan pays 80 basis points over all. Ms. Van Liew reviewed the differences between a consulting model and a manager of managers model. The manager model will typically save 10 – 20% in costs. The Retirement System would have an agreement with Northern and in turn Northern would then have responsibility of hiring managers. Northern can become co-fiduciary and possibly co-trustee of the plan.

Northern monitors their managers daily. Continuous evaluation and manager selection philosophy leads to strong performance. Northern believes in asset allocation, research, diversification, monitoring and rebalancing. Northern is able to change their managers in approach as needed. Northern would likely have 23 underlying managers compared to current number of about 10. Northern has outperformed their benchmark on average for every client by 1.91% for the past 5 years with the goal to exceed the benchmark by 100 – 150 basis points.

Northern would use active managers more than passive. Mr. Jaffe asked what would cause Northern to fire a manager without consulting the Board first. Ms. Van Liew indicated a significant change in management style and she expressed the importance of continued communication with relationships. The Board would have access to local Northern representatives as well. Ms. Van Liew would not give asset recommendations without a full asset study.

Northern composite performance is gross of fees. Ms. Jensen indicated the Fund would need independent monitoring every three years. Mr. Cuomo asked about the difference in approach from Prime Buchholz. Ms. Van Liew explained that Northern has a higher degree of accountability due to involvement of manager selections. Northern can give as much education to the Trustees as desired. It was discussed that Northern could share fiduciary liability but that the Board would not be absolved from it. Mr. Geisler expressed concern over the number of managers recommended, that too many managers can water down the *alpha*. Ms. Van Liew stressed that a diversified strategy leads to stronger, not weaker performance.

Mr. Cuomo expressed he would like to explore the concept further as well as the other Trustees.

John Cuomo motioned to put together an RFP for a manager of managers. Robert Jaffe seconded the motion, passed by the Trustees 4 – 0.

Richard Krock recommended 3 presenters. Mr. Jaffe wanted to explore a larger number of institutions rather than invite only 3.

The question arose where to advertise the RFP. Ms. Jensen suggested P & I. Mr. Cuomo wants 3 weeks to review the responses before the next meeting. Ms. Jensen suggested holding a special meeting in 2 months to consider the issue and that she could draft an RFP by the first week of March.

Northern offered to share their RFP as a template. Mr. Krock does not feel the approach really cedes that much control, while it is the Board's responsibility to decide what contracts would be relieved. Ms. Jensen replied that the manager of managers must meet requirements of statute and investment policy and that the Board must still have an independent evaluation every 3 years.

Mr. Jaffe stated he would like to end the meeting at 12:30 PM.

VII. QUARTERYLY INVESTMENT REPORT: PRIME BUCHHOLZ – RAMELLE HEIRONYMOUS & SEAN HIGMAN

Sean Higman introduced himself again to the Board. He has 18 years experience as a plan sponsor with oversight for up to $1 billion in assets. Mr. Higman added that asset liquidity studies rarely add much insight. Mr. Higman clarified that Jon Prime has begun the process to retire and other partners will transition ownership over an extended period of time.

Mr. Higman takes exception to the comparison of Prime Buchholz to manager of managers. Prime Buchholz sees the role very much like a manager of managers with the exception that the firm will not aid in discretionary capacity. Prime Buchholz has a very simple agreement with the Board allowing the Board the option to move if ever necessary. Mr. Higman would like the actual performance in the RFP. Mr. Higman's own experience with a manager of managers is that the story is compelling but the actual experience is often mediocre.

Ms. Hieronymus added concern about the ability of traditional asset classes to meet objectives of the Plan. Mr. Higman said that typically broader diversification leads to higher returns and lower volatility.

A. QUARTERLY PERFORMANCE REPORT

Mr. Higman reported the portfolio returned 2% for the quarter ending December 31, 2005, bring the gain for the year to 5.7% and the fund assets totaled $47,996,557. The performance trailed the Target Index and the Actual Index but was ahead of the 60/40 composite benchmark. With 3 years of performance the plan has returned 11.5% (when Prime Buchholz was hired) versus 12.3% for the new index.

Mr. Krock asked why we even bothered with the old 60/40 index since the plan failed to meet its new objectives; the old index is irrelevant. Mr. Higman responded that 10% is manager selection and 90% is asset allocation, so the performance of the Retirement System was improved by asset allocation. Mr. Higman stressed the value added by Prime Buchholz with respect to the change in asset allocation. Mr. Jaffe stated the objectives are to protect the assets and maximize returns. The plan needs to meet the objectives.

Mr. Krock questioned how we could have a target return that comes under the actuarial assumption. Mr. Higman explained the Board can only expect to exceed returns over a period of time.

B. REVIEW ASSET ALLOCATION AND INVESMENT MANAGER RECOMMENDATIONS

Mr. Jaffe asked if changing the assumption would change the funding by the Town. Mr. Higman added the Board could achieve returns of 8% or better over time, although not *all* the time. 8% is the most common assumption for similar plans. Mr. Higman believes the asset allocation should achieve 8% over time, but only during many time periods, the plan will both exceed and perform under the objective. Mr. Krock asked for clarification of the 10-year actuarial index, which Mr. Higman explained represents the actual asset mix for the plan. Mr. Higman also explained that the index did not include fees.

Mr. Cuomo asked about Callahn, that Prime Buchholz originally represented that the Fund under performed once in 8 years though Prime Buchholz has yet to beat Callahn compared to the General Employees. Mr. Higman responded 3 years is not long enough to properly evaluate the decision. The Board needs a full business cycle to judge the asset allocation. Mr. Cuomo then stated that the Fund did not even beat Callahn for one year. Mr. Cuomo understood that the Fund should do better with the new allocation and also do better than the target. Mr. Cuomo stated that he is not an investment professional, the Board hired Prime Buchholz and ever since that decision, the performance has not met expectations. Mr. Higman explained the portfolio is designed to produce performance with reduced volatility and results will vary.

Mr. Jaffe stated the only thing that matters to the Board is how they perform and their objective should always be to outperform for every period.

Mr. Krock noted the Board cannot wait 8 years to see if they are wrong. Mr. Higman responded that statistically they will only outperform half of the time. The Board has a return of 5.7% net of fees versus the index at 6.2% gross of fees.

VIII. ATTORNEY REPORT

A. STATUS OF LEGG MASON AND STRALEM CONTRACTS

Ms. Jensen stated the Stralem contract has been executed. Legg Mason specifically will not acknowledge a fiduciary to the Plan and she does not recommend the Board to execute the application. Ms. Jensen noted the other managers acknowledge a fiduciary. Mr. Krock stated that if Ms. Jensen does not recommend signing the contract he would refuse to sign.

Ms. Hieronymus recommended dividing the Torray fund between Stralem and the S&P 500.

Mr. Cuomo motioned to liquidate the Torray fund, dividing the proceeds between Stralem and the S&P 500. Mr. Geisler seconded the motion, passed by the Trustees 5 – 0.

B. PERMISSIBLE INVESTMENTS

Ms. Jensen noted that the current Investment Policy Statement has conflicting provisions. Prime Buchholz recommended changing to 5% International to conform to statute.

Jaffe motioned to amend the Investment Policy to comply with statute. Mr. Hayes seconded the motion, passed by the Trustees 5 – 0.

The Board decided to wrap up the rest of the agenda at special meeting called March 16th.

IX. RETIREMENT APPLICATIONS: BENEFIT APPROVALS

Mr. Jaffe motioned to accept the benefit approvals and Mr. Geisler seconded the motion, passed by the Trustees 5 – 0.

X. SELECTION OF A VICE-CHAIRMAN

Mr. Jaffe motioned to select Peter Geisler as the Vice-Chairman. The motion was seconded by Mr. Krock, passed by the Trustees 5 – 0.

XI. ADJOURNMNENT

There being no further business, a motion was made, seconded, and passed 5-0 to adjourn the meeting at 12:17 PM.

Approved: ________________________________