TOWN OF PALM BEACH

Office of The Town Clerk

MEETING TO DISCUSS
POTENTIAL COMMINGLING OF
FOUR TOWN TRUST FUNDS
FOR INVESTMENT PURPOSES ONLY

SEPTEMBER 22, 2006 at 9:00 A.M.

I. CALL TO ORDER

The meeting was called to order at 9:00 a.m. by Town Manager Peter B. Elwell. Those present were:

Dr. Michael Andrews - Chairman, Investment Advisory Board
Scott Baur - Administrator for Police and Firefighter Boards
William Crouse - Human Resource Director and Administrator General Employees Board.
Peter B. Elwell - Town Manager and Member of General Employees Retirement Board
Robert Garvy - Chairman, General Retirement Board of Trustees
Bonnie Jensen - Counsel for Firefighters Retirement Board of Trustees
Robert Klausner - Counsel for Police Retirement Board of Trustees
Richard Krock (via telephone) - Chairman, Firefighters Retirement Board of Trustees
John McCracken - Counsel for General Retirement Board of Trustees
Raymond Snow - Chairman, Police Retirement Board of Trustees
Jane Struder - Finance Director

II. INTRODUCTION OF TOPIC

Mr. Elwell explained that meeting in a formal manner was in accordance with the Florida Sunshine Law. Both he and Robert Garvy were participating in the meeting, and since both were members of the General Employees Retirement Board of Trustees, this had to be a public meeting. He explained that he had come before each of the retirement boards to describe an opportunity to consolidate the funds from each of the three different retirement funds, and the Town trust fund being created for the long term retiree health insurance coverage provided by

Post Office Box 2029 • 360 South County Road • Palm Beach, Florida 33480
Telephone (561) 838-5416 • Facsimile (561) 838-5417
E-mail: townclerk@townofpalmbeach.com • Website: www.townofpalmbeach.com
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the Town. The funds assembled would total over $180 million, as opposed to being less than $20 million for the Health Fund, and $50 to $65 million for each of the three Retirement Funds.

Mr. Elwell stated that the goal was to manage the funds in a way that would preserve the security of the benefit for all participants in the three different retirement programs, and the health trust, while controlling the increasing costs that had been a burden to the taxpayers. He noted that the plans would remain separate, however, consideration of the advantages of pooling funds, for investment purposes only, would be the focus of the discussion today.

III. INTRODUCTION OF MEETING PARTICIPANTS

The members in attendance introduced themselves.

IV. GENERAL DISCUSSION OF THE "UMBRELLA INVESTMENT COMMITTEE" CONCEPT

Mr. Snow, on behalf of the Police Retirement Board, stated that there had been some concern expressed as to a sense of disenfranchisement, however, with a limited knowledge, there was willingness to learn about the concept.

Attorney Klausner added that there was some independence that each fund would need, and there was an economy of scale that would go with unification. In addition to looking at performance, the actuarial issues would also need to be reviewed. The biggest driver for costs for defined benefit retirement systems came from the actuarial assessments, in which the primary factors were salary and investment returns. There were different demographics in each of the three retirement plans in terms of age and longevity of employment, which would affect the cash flow needs of the plans.

Mr. Garvy, on behalf of the General Employees Board, reaffirmed the concern of a separation or perceived distance being established between the membership and the ultimate asset allocation, and the potential conflicts of the risk appetite of one group of participants versus another. There were clearly some significant advantages in terms of efficiency and availability of investment alternatives when funds were combined.

Mr. Krock, on behalf of the Firefighters Retirement Board, commented that the general feeling was favorable to the overall concept.

V. IDENTIFICATION OF SPECIFIC LEGAL, TECHNICAL, AND LOGISTICAL ISSUES TO ADDRESS

Mr. Elwell explained that the fiduciary responsibility and roles of the boards would need to be explored. There were also the unique requirements of Chapter 175 and Chapter 185, of the Florida Statutes, which would require specific reporting and accounting requirements. While the funds may be pooled in order to obtain the best return on behalf of everyone who was involved, the accounting would need to be separate for each of the retirement boards.

Attorney Klausner commented that as long as the decision by the police and fire representatives would ultimately receive some act of ratification, satisfying the Division of Retirement, the boards remained ultimately responsible for administration of the plan. Florida law provided that the board of trustees of each plan was ultimately responsible for management and control of the assets of the plan, but there were a number of retirement plans in Florida that had pooling arrangements for investment. The creation of an investment agreement, a three-party mutual fund, would pool the assets and report the results to each board for ratification. If the board found that the overall return was less favorable in the pooling arrangement than it was in a stand alone situation, the board could withdraw from the arrangement. The board remained ultimately responsible in collective investment arrangements of independent funds, that were accepted by the Division of Retirement as long as the board had the ability to withdraw if necessary.

Attorney Klausner explained that the hardest part would be coming to a collective agreement on the financial side, as to what the investment philosophy would be. There were some limitations within Florida law in terms of what investments could be made, and a larger pool would allow entry into the alternative investment area, at least in certain percentages of the portfolio that would not be available otherwise in smaller funds. The real work would be on setting an investment policy that everyone could live with. The investment policy should be worked out within this committee structure of the three funds, but each board would need to ratify the investment policy as its own in order to exercise the necessary fiduciary oversight that each board would retain, and to satisfy the ultimate concern that the risk parameters were good for everyone.

Attorney Jensen commented that the concept of a commingling that the boards would invest together was the step in the right direction, rather than removing from the board the entire decision making process. Each board would need to retain the ability to review and ratify the investment, as well as have the opportunity to opt out if the investments did not meet their requirements.

Mr. Elwell replied that the concept of the boards staying engaged, rather than simply receiving information addressed many of the concerns he had heard previously. He requested clarification of the term "ratification," as to whether the boards would be passing judgment quarterly or on some other cycle on what the Umbrella Committee was doing, or whether the boards would simply be monitoring carefully, in their fiduciary role, what was going on at that level.

Attorney Klausner suggested that the Umbrella Committee would work out a collective investment policy, which would need to be adopted by each board. Each board should receive a report of the Committee's investment results quarterly, just as the Committee would. The boards would then continue to oversee the investments, and if not satisfied could opt out. As long as those powers were retained, that is, directly approving the creation or any material investment of the investment policy, and the decision to stay or go, the boards could delegate direct operation of the investments to the Umbrella Committee. Each board would have the duty to review the quarterly results of the collective investment pool, in order to satisfy the legal requirements.

Attorney Jensen agreed, and commented that the ratification process would be what each board decided that ratification process was going to be, with as much information as they needed in order to continue with the investment.

Mr. Elwell clarified that the ratification would then not be of the individual investments, but rather of the process, and that process would be ongoing and closely monitored by each of the boards. Any board that became dissatisfied with the process could opt out. The boards would not be quarterly ratifying the activity of what was happening at the Umbrella Committee.

Attorney Klausner replied that the Umbrella Committee would decide which investments would be made. If there was a material shift in the investment policy, statutory requirements would require the investment policy to go back to each board to be approved.

Mr. Elwell noted that, by Town ordinance, the policy would need to be adopted by the Town Council.

Dr. Andrews clarified that from the Investment Advisory Committee's standpoint, it was important to differentiate the ratification between the investment and the investment policy.

Mr. Snow commented that a key element in the whole process was the broader issue of alternative investments, and there were some who believed that alternative investments were not only desirable, but necessary as a moderator of volatility. The ability to withdraw, in the case of alternative investments, may become problematic.

Mr. Garvy pointed out that, from a legal standpoint, the Committee may be comfortable with the individual board participants to opt in or out of the commingled funds, however, he questioned whether there would be opportunity offered to each board to express their risk appetite by choosing which level of unit values they wanted.

Attorney Klausner remarked that he would be willing to draft an agreement, both ways: with everyone putting all of their funds in, with the question being were you all in with one investment policy, or were you all in with a menu. Either way would allow a large pool of money to create greater opportunities for investment, while also creating a greater opportunity for a comfort level for the individual funds themselves. The draft document would allow the Committee to work from a concrete set of starting points.

Mr. Garvy clarified that his suggestion was that the fund would put 100% of their funds in the investment pool, but would elect that 40% of that be in alternatives, such as 10% in aggressive equities, 30% in fixed income, etc., which might be in considerable contrast to the Investment Advisory Committee, which dealt with short term investments of the Town, for example, 90 day Treasury Bills.

Mr. Baur commented that an advantage of unitizing the investments individually would maintain greater board control. An advantage to unitizing the collective whole was managed cash flow, as the cash inflow of one plan would end up funding the outflow of another plan, while maintaining greater stability of the invested assets.

Mr. Elwell suggested that anyone who wanted to make suggestions, or provide information to Mr. Klausner could do so.

In reply to Mr. Elwell, Mr. Garvy commented that the risk profile that would emerge from the larger pool would differ from the individual board funds. The correlation of how the fund managers would relate to each other would create a more favorable risk/return relationship than would be evident at the single manager level. The compelling reason for the Umbrella Committee was that, presumably, the Committee would have a greater degree of multiple expertise available to it, and that it could mix the manager in such a way that the risk profile for the expected return was more favorable than it would be with each board operating independently.

Mr. Elwell commented that the idea was to take the best investment talent available from each of the participating boards, and put them together as the Umbrella Committee. It was proposed to be five members, in part so that the Committee could operate at an expert investment level to make decisions together. Each of the three retirement boards, would have one representative, chosen by the board, one representative from the Investment Advisory Committee, and a fifth person to be appointed by the Town Council. Once the Umbrella

Committee was created, it would decide how frequently it would meet, and the individual boards would need to act accordingly to provide the oversight and input necessary.

Attorney McCracken noted that the proposed format of the Umbrella Investment Committee would change the dynamic of those wishing to serve on each individual board dramatically, and suggested that consideration be given to having two representatives from each of the boards on the Umbrella Investment Committee.

Mr. Garvy expressed concern that the Umbrella Investment Committee exceed five members, as the larger the committee, the less effective it may be.

Mr. Elwell noted that the pros and cons of a smaller versus a larger group could be assessed.

VI. OTHER COMMENTS/QUESTIONS ON THE SUBSTANCE OF THIS MATTER

In response to Dr. Andrews, relative to the administration of the Umbrella Investment Committee, Mr. Elwell replied that was a detail that could be discussed as the structure of the Committee was formed, however, Town staff was prepared to provide the staffing for the Umbrella Investment Committee. Mr. Elwell noted that it would be necessary to hire a set of professionals to manage the money and account for the money as a custodian, however, Town staff could provide the administrative coordinating functions.

VII. WHAT MUST BE DONE (AND WHO WILL DO IT) TO PREPARE FOR OUR NEXT MEETING

In prior discussion today, it was determined that Attorney Klausner would draft a document for creating the structure of the pooling of the funds for review at the next meeting. Staff would obtain information from the different funds of the fee structures for assessment of the economies of scale.

Mr. Garvy suggested that the break points for the managers be reviewed, considering that each of the asset classes were likely to have more than one manager, not a single manager.

Attorney Klausner stated that he would e-mail the draft document to the Town Manager for distribution.

Mr. Elwell commented that the document would be reviewed at the next meeting, for review by the boards at the November quarterly meetings.

VIII. IDENTIFICATION OF DATE, TIME, AND PLACE FOR THE NEXT MEETING

The next meeting was scheduled for Thursday, October 19, 2006, at 3:00 p.m., with the location to be determined. Mr. Krock noted that he would be available that day by teleconference.

IX. ADJOURNMENT

The meeting was adjourned at 10:37 a.m.

SUBMITTED BY:

Peter B. Elwell
Town Manager